Supreme Court, U.S.
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12 No. 08-1

In The

Supreme Court of the United States

RICHARD MADSEN and NANCY MADSEN,

Petitioners,

vs.

JP MORGAN CHASE BANK, N.A.,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Court Of The State Of Utah

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether federal regulations (12 C.F.R. §§ 541.5, 544.1, and 545.6-11(c)) barring the payment of interest on escrow funds "except as provided by contract" preempt Utah law (as set forth in *Madsen I*, herein) holding that the banks must pay profits earned on "pledged" funds.

2. Whether this Court should warn courts and counsel to address the issue of federal preemption early in the case, saving as much as 34 years in futile litigation.

LIST OF PARTIES

Pursuant to Rule 14.1(b), the following list identifies all of the parties to the appellate proceeding in the Supreme Court of Utah, whose judgment is sought to be reviewed:

A. Petitioner

Nancy Madsen, for herself and all others similarly situated.

Richard Madsen was a named party, but died before this matter last came before the Utah Supreme Court. Likewise, many other members of the class have died, and their heirs are the interested parties.

B. Respondent

Washington Mutual Bank fsb ("WAMU") was the defendant named when this matter last came before the Utah Supreme Court.* It was the successor in interest to Olympus Federal Savings and Loan, which succeeded Prudential Federal Savings and Loan.

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* This case was originally filed against Prudential Federal Savings & Loan Association. Later Prudential was sold to Olympus Federal Savings & Loan Association. Still later Olympus was purchased by Washington Mutual Bank fsb. According to fn. 1 in the trial court's *Final Judgment Dismissing Action with Prejudice*, "JP Morgan Chase Bank, N.A. is the successor in interest to Washington Mutual Bank fsb." However, nothing has been filed by the defendant to explain the term "successor in interest." Herein all of the above will be referred to simply as "the Bank".

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OPINIONS AND ORDERS BELOW

The decision of the Utah Supreme Court sought to be reviewed is reported at 199 P.3d 898 (Utah 2008), and reprinted in the Appendix A ("App. A"). The prior reported decisions on this matter are found at 558 P.2d 1337 (Utah 1977), 635 F.2d 797 (10th Cir. 1980), *cert. denied*, 451 U.S. 1018 (1981), and 767 P.2d 538 (Utah 1988), and are reprinted at App. F, E, and D, respectively.

JURISDICTION

The Supreme Court of Utah rendered its decision on September 23, 2008 (App. A), and denied a timely petition for rehearing on December 5, 2008 (App. G). This Court has jurisdiction under 28 U.S.C. § 1257(a).

PERTINENT CONSTITUTIONAL, STATUTORY, AND REGULATORY PROVISIONS

The pertinent constitutional, statutory, and regulatory provisions are set forth in the Appendix at App. H, specifically including 12 C.F.R. §§ 541.5, 544.1, and 545.6-11(c).

STATEMENT OF THE CASE

1. This case was filed in February 1975 (**34 years ago**). It may be the oldest case for civil damages in the United States.

2. This case began when Madsen borrowed money from the Bank[1] to purchase a home. As part of his monthly mortgage payment, the trust deed contract required Madsen to make a monthly payment towards future property taxes and insurance. At year's end, the Bank would pay the annual property taxes and insurance on behalf of Madsen. The contract provides:

> In addition to the monthly payments as provided in said note the TRUSTOR agrees to pay to the beneficiary, upon the same day each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to be adjusted from time to time as required, and *said budget payments are hereby pledged to the BENEFICIARY* as additional security

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[1] This case was originally filed against Prudential Federal Savings & Loan Association. Later Prudential was sold to Olympus Federal Savings & Loan Association. Still later Olympus was purchased by Washington Mutual Bank fsb. According to fn. 1 in the trial court's *Final Judgment Dismissing Action with Prejudice*, "JP Morgan Chase Bank, N.A. is the successor in interest to Washington Mutual Bank fsb." However, nothing has been filed by the defendant to explain the term "successor in interest." Herein all of the above will be referred to simply as "the Bank".

> for the full performance of this deed of trust and the note secured hereby. The budget payments so accumulated may be withdrawn by the BENEFICIARY for the payment of taxes or insurance premiums due on the premises.

Madsen v. Washington Mutual Bank fsb, 199 P.3d 898, 900 [¶3] (Utah 2008). (*Madsen IV*) (Emphasis added.)

3. However, the Bank did not *hold* the funds until year's end. Rather the Bank invested those funds and earned a secret profit while waiting to make the annual payment for taxes and insurance. Madsen sued the Bank (class action). Madsen claimed that profits or interest from investing the "pledged" funds belonged to Madsen.

4. In 1977, the case went before the Utah Supreme Court. (*See* Appendix F.) (Also referred to herein as *Madsen I*.) In *Madsen I*, the Utah Supreme Court held, *inter alia*, that:

> The essential elements of a pledge are contained in the agreement . . .
>
> * * *
>
> [W]hen the property pledged is of such a character as not to be lessened by use, the pledgee does not incur liability by using it; but, if from the use of it profits are derived, pledgee must, in the absence of a special agreement, account for them to the pledgor.
>
> * * *

> The pledgee has the duty to account to the pledgor for the increase or profits accruing to the pledgee as a result of the possession of the pledged chattel.

558 P.2d at 1339-40. (*See* App. F5, F6, F8.)

5. After the ruling in *Madsen I* (¶4 above), the Bank filed a declaratory judgment action in federal court. The Bank also filed a petition to remove the state court case to federal court. The central theory of both federal actions was that Madsen's state law contract claims had been preempted by federal law. The federal trial court ruled in favor of the Bank and dismissed the case.

6. The case was appealed to the Tenth Circuit Court of Appeals. (*See* Appendix E). (Also referred to herein as *Madsen II*.) In *Madsen II*, the Tenth Circuit Court of Appeals reversed the federal district court and sent the case back to state court. The Tenth Circuit held *inter alia*:

> [W]e hold that state law is applicable in determining whether Prudential contracted to pay interest on the Madsens' escrow account.
>
> * * *
>
> [T]he most one can say is that a question of federal law is lurking in the background.

Madsen v. Prudential Sav. & Loan Ass'n, 635 F.2d 797, 803-04 (10th Cir. 1980). (*See* App. E13, E16.)

7. After the case was remanded back to state court, the trial court made rulings not relevant here. The case was again appealed to the Utah Supreme Court. (*See* Appendix D.) (Also referred to herein as *Madsen III*.) The Utah Supreme Court ruled in Madsens' favor and remanded back to the Utah State trial court.

8. After the appeal in *Madsen III*, a lengthy trial was held in the state trial court. The trial court judge entered a Final Judgment of approximately $1,000,000.00 on behalf of approximately 10,000 class members. (Appendix B.) The Bank appealed. The Utah Supreme Court reversed the trial court and dismissed the case with prejudice. (*See* Appendix A.) (Also referred to herein as *Madsen IV*.)

9. In *Madsen IV*, the Utah Supreme Court held as follows:

> WAMU [the Bank] argues that 12 C.F.R. § 545.6-11(c) . . . preempts any state law under which the Madsens might recover. That section reads as follows:
>
> * * *
>
> *. . . Except as provided by contract, a Federal association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph.*
>
> Under this regulation, Prudential had no obligation to pay interest to the Madsens absent a . . . contractual obligation to the

> contrary. *The Madsens' accounting claim is not founded on a contract* . . . (Emphasis added.)
>
> * * *
>
> *And in the absence of a contract* . . . the regulation is clear that Prudential had no obligation to pay interest. (Emphasis added.)
>
> * * *
>
> [W]e . . . hold that federal law preempts the Madsens' accounting claim, and remand with instructions to enter summary judgment in favor of WAMU.

199 P.3d 898, 904, 907 [¶¶21, 22, 32, 33].

REASONS FOR GRANTING THE WRIT OF CERTIORARI

1. CERTIORARI SHOULD BE GRANTED TO PUT A STOP TO UNNECESSARY AND HUGE DELAYS WHERE FEDERAL PREEMPTION IS AN ISSUE.

Federal preemption is the ultimate "trump card." Simply stated, if a case is filed in state court, based upon state law, the case is ended if federal preemption applies.

But are state courts looking at federal preemption issues in the *beginning*, or in the *middle*, or at the *end* of the case? In the case at bar, the Utah Supreme Court looked at the federal preemption

issue at the *end* of the case, and **34** years were wasted. And hundreds or probably thousands of hours of judicial time was wasted.

Of course, there are thousands and thousands of other cases pending in courts throughout the United States where federal preemption is an issue. And if judges in those cases delay ruling on preemption, until somewhere in the *middle* or the *end* of the case, **millions of judicial hours will be wasted.**[2]

In summary, certiorari should be granted, so that this Court can give a *stern warning* to lawyers and judges, throughout the land, that issues of federal preemption should be heard in the beginning of a case; and not delayed until the *middle* or the *end* of the case.[3]

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[2] Of course, judges have a variety of "tools" available to push issues of federal preemption to the forefront of the litigation. The most basic "tool" is very simple: Where several issues or motions are pending before the court, the court should simply put preemption issues at the top of the list. Other "tools" to push preemption to the forefront might be Rule 16, *Federal Rules of Civil Procedure* (basically equivalent to Rule 16, *Utah Rules of Civil Procedure*) or Rule 54(b), *Federal Rules of Civil Procedure* (basically equivalent to Rule 54(b), *Utah Rules of Civil Procedure*).

[3] Petitioner is *not* asking this Court to rule on *why* issues of federal preemption were delayed for **34** years in this case. (However, petitioner believes Utah courts did not use the "tools" mentioned in fn. 2 above.) Rather, petitioner simply seeks a ruling that the Utah Supreme Court's *ultimate* decision on federal preemption, after **34** years, was incorrect. But certiorari would also give this Court an opportunity to warn about delays,

(Continued on following page)

2. CERTIORARI SHOULD BE GRANTED BECAUSE THE RULING OF THE UTAH SUPREME COURT (IN *MADSEN IV*) CONFLICTS WITH FEDERAL APPELLATE DECISIONS.

The ruling of the Utah Supreme Court in *Madsen IV* (¶9 above) squarely conflicts with the ruling of the Tenth Circuit Court of Appeals in this very *same* case. (*See Madsen II* at ¶6 above.) In *Madsen II*, the Tenth Circuit Court of Appeals ruled that:

> Here the basic issue in the Madsens' complaint is whether *the contract between the Madsens and Prudential* requires the payment of profits or interest on escrowed funds. (Emphasis added.)
>
> * * *
>
> [W]e hold that *state law is applicable* in determining whether Prudential contracted to pay interest on the Madsens' escrow account. (Emphasis added.)

635 F.2d at 801, 803. (*See* App. E9, E13.)

The conflict is obvious. In *Madsen II*, the Tenth Circuit Court of Appeals concluded that there *was* a contract (viz. "trust deed") between Madsen and the Bank; but that the contract had to be interpreted and construed by "state law." However, in *Madsen IV*, the

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in general, where federal preemption is an issue. And certiorari would give this Court an opportunity to encourage lower courts to use tools *they already have* to push federal preemption to the forefront of the litigation. (*See* fn. 2 above.)

Utah Supreme Court concluded that there was *no* contract[4] and thus nothing to interpret.

The ruling of the Utah Supreme Court, in *Madsen IV* (¶9 above) also conflicts with *Altria v. Good*, ___ U.S. ___, 129 S.Ct. 538 (2008). In *Altria*, the United States Supreme Court ruled as follows:

> [T]he historic police powers of the States are not to be superseded by the Federal Act unless that is the clear and manifest purpose of Congress. Thus, when the text of a pre-emption clause is susceptible of more than one plausible reading, courts ordinarily accept the reading that disfavors pre-emption. (Internal quotation omitted.)

129 S.Ct. at 543.

The conflict between *Madsen IV* (¶9 above) and *Altria* is simple and straight forward. In *Madsen IV*, the entire opinion (and the dismissal of the class action) was based upon the Utah Supreme Court's ruling that: "*The Madsens' accounting claim is not founded on a contract . . .* " 199 P.3d 898, 904 [¶22]. (Emphasis added.)

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[4] The federal regulation at issue (12 C.F.R. § 545.6-11(c)) states: "Except as provided by contract . . . " (*See* App. H21.) But note that the regulation does *not* say: "Except as provided by *express* contract . . . " However, even if an *express* contract is necessary, the contract in this case *expressly* states that Madsen's payments were "pledged" to the Bank. (*See* ¶2 above.) And the case of *Madsen I* interprets and construes the legal effect of such a "pledge."

But obviously there is a written contract (viz. "trust deed") between the parties; and in the case of *Madsen I* (¶4 above), the Utah Supreme Court gives a lengthy and detailed interpretation of that written contract. Or stated in other words: in 1977 the Utah Supreme Court said there *was* a contract, but in 2008 the Utah Supreme Court said there was *no* contract. (*See* ¶9 above.)

But according to *Altria*:

> [W]hen the text of a pre-emption clause is susceptible of more than one plausible reading, courts ordinarily accept the reading that disfavors pre-emption.

129 S.Ct. at 543.

In short, in 1977, the Utah Supreme Court interpreted the federal regulation in a way that <u>*dis*</u>favors preemption. But in 2008, the Utah Supreme Court interpreted the federal regulation in a way that <u>*favors*</u> preemption. (*See* fn. 4 above.)

Respectfully submitted,

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APPENDIX A

199 P.3d 898

Supreme Court of Utah.
Richard MADSEN and Nancy Madsen,
for themselves and all others similarly situated,
Plaintiffs, Appellants, and Cross-Appellees,
v.
WASHINGTON MUTUAL BANK FSB, (successor to
Prudential Federal Savings and Loan Association),
Defendant, Appellee, and Cross-Appellant.
No. 20060597.

Sept. 23, 2008.
Rehearing Denied Dec. 5, 2008.

Robert J. Debry, Lynn P. Heward, Salt Lake City, for plaintiffs.

Joseph J. Palmer, Stephen C. Tingey, Elaina M. Maragakis, Salt Lake City, for defendant.

DURRANT, Associate Chief Justice:

INTRODUCTION

¶ 1 In 1964, Richard and Nancy Madsen financed the purchase of their home by borrowing money from Prudential Federal Savings and Loan Association ("Prudential") under a real estate mortgage contract. The contract obligated the Madsens to make monthly payments into an account held by Prudential for the purpose of paying taxes and insurance premiums. Prudential paid no interest or earnings on the running account balance. The Madsens sued, seeking

interest on their account. This case requires us to decide whether the Madsens may recover, on a common law accounting theory, profits that Prudential and its successor, Washington Mutual Bank ("WAMU") may have earned from the use of the funds, or whether federal law preempts the Madsens' claim. We hold that federal law preempts the Madsens' claim.

BACKGROUND

¶ 2 This is the third appeal before us in the protracted history of this case, which was initiated more than thirty years ago. And although we have twice ruled in this case on appeal, our analysis of the issues requires a full explanation of the facts and procedural history.

¶ 3 The facts forming the basis for the Madsens' claim are not in dispute. In 1964, the Madsens borrowed money from Prudential to finance the purchase of their home. The standard form trust deed used by Prudential required the Madsens, as trustors, to make monthly "budget payments" into an account held by Prudential, the trustee and beneficiary of the trust deed:

> In addition to the monthly payments as provided in said note the TRUSTOR agrees to pay to the beneficiary, upon the same day each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to

> be adjusted from time to time as required, and said budget payments are hereby pledged to the BENEFICIARY as additional security for the full performance of this deed of trust and the note secured hereby. The budget payments so accumulated may be withdrawn by the BENEFICIARY for the payment of taxes or insurance premiums due on the premises. The BENEFICIARY may at any time, without notice, apply said budget payments to the payment of any sums due under the terms of this deed of trust and the note secured hereby or either of them.

The trust deed did not contain any provision requiring Prudential to pay interest or profits on the budget payments, and Prudential paid none.

¶ 4 In 1975, the Madsens sued Prudential as the representatives of a class of borrowers who, like the Madsens, made budget payments to Prudential under the terms of their trust deeds. The Madsens brought a claim for breach of contract and sought an accounting of interest or profits under a theory of unjust enrichment (the "accounting claim"). The Madsens argued that Prudential was unjustly enriched because the budget payments were held as a pledge and the common law required Prudential, as pledgee, to account for any profits earned through the use of the pledge.

¶ 5 After the district court certified the class, Prudential sought judgment as a matter of law. In separate motions, Prudential moved the court to dismiss

or grant summary judgment in its favor. In both motions, Prudential argued that federal law, which specifically authorized Prudential to hold budget payments without paying interest, preempted the Madsens' accounting claim. Furthermore, in one of its motions, Prudential argued that the contract, which was complete and unambiguous, contained no provision obligating Prudential to pay interest.

¶ 6 The district court granted summary judgment to Prudential on its contract claim without addressing its preemption claim. The court reasoned that "neither the contract provisions, express or implied, the principles of 'unjust enrichment,' nor those of 'pledges' give to plaintiffs a claim upon which relief can be granted on the contract in question." The Madsens appealed, and we took up the case in *Madsen v. Prudential Federal Savings & Loan Ass'n ("Madsen I")*.[1] We reversed, holding that the funds deposited under the loan agreement satisfied the essential elements of a common law pledge: "The essential elements of a pledge are contained in the agreement, viz., the existence of a debt or obligation, a transfer of property to the pledgee, to be held as security and, if necessary, to be used to assure performance of the obligation."[2] We held that the common law of pledge required that "if from the use of [the pledge] profits are derived, pledgee must, in the absence of a special

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[1] 558 P.2d 1337 (Utah 1977).

[2] *Id.* at 1339.

agreement, account for them to the pledgor."[3] Thus we remanded the case to the district court to consider the Madsens' accounting claim.

¶ 7 Although Prudential referred to federal banking regulations as part of its policy argument in its appellate brief to us, Prudential did not argue federal preemption. Accordingly, our decision did not address federal banking regulations or federal preemption. Nor did our decision address the Madsens' claim for breach of contract. Instead, we confined our decision to whether the budget payments constituted a common law pledge.[4] We reversed the district court's grant of summary judgment, holding that the budget payments were such a pledge and that the Madsens could pursue their accounting claim.[5]

¶ 8 Following the remand, Prudential removed the case to federal district court, asserting, as a basis for federal jurisdiction, that the case involved an important question of federal law. The Madsens moved for dismissal, arguing that the federal court lacked jurisdiction. When the federal district court denied the Madsens' motion to dismiss, the Madsens appealed to the United States Court of Appeals for the Tenth Circuit in *Madsen v. Prudential Federal Savings & Loan Ass'n ("Madsen II").*[6] The Tenth Circuit

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[3] *Id.* at 1340.

[4] *Id.* at 1339-40.

[5] *Id.*

[6] 635 F.2d 797 (10th Cir.1980).

reversed, holding that "Prudential's claim of federal preemption is in the nature of a defense to the Madsens' cause of action and cannot be the basis of federal question jurisdiction on removal."[7] The case was remanded to the state district court.[8]

¶ 9 On remand in the state district court, Prudential revived the federal preemption argument in a new motion for summary judgment. In reply, the Madsens alleged that although we did not mention the federal preemption issue in our ruling, we had already decided the issue in the Madsens' favor in *Madsen I.* The Madsens further argued that the issue was decided in their favor by the Tenth Circuit in its ruling that the federal court had no jurisdiction. After a hearing, the district court ruled simply, "Prudential's Motion for Summary Judgment based upon federal preemption is hereby denied," offering no further explanation.

¶ 10 The parties proceeded to try the "test case" of Prudential's liability. Judge Kenneth Rigtrup limited the trial to the issue of whether Prudential earned profit from the use of the Madsens' pledged funds and, if so, how much. Because he narrowed the scope of the trial to this one issue, he did not allow Prudential to present evidence or argue in support of several defenses that it had urged. He did not allow Prudential to argue federal preemption or introduce evidence

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[7] *Id.* at 802.

[8] *Id.* at 804.

of a "special agreement" whereby the parties agreed that no interest would be paid. He then ruled in favor of the Madsens, awarding them $134.70 plus interest from the date of judgment on their individual claim.[9]

¶ 11 Prior to the trial and again prior to issuing his ruling, Judge Rigtrup disclosed to the parties that he was a potential class member, having financed the purchase of his own home by borrowing from Prudential.[10] Thirty-nine days after this ruling, Prudential moved to disqualify Judge Rigtrup. The presiding judge granted Prudential's motion, and the Madsens sought permission to file an interlocutory appeal.[11]

¶ 12 We granted such permission and addressed Judge Rigtrup's disqualification in *Madsen v. Prudential Federal Savings & Loan Ass'n ("Madsen III")*.[12] We held that Prudential's motion to disqualify was not timely.[13] We also ruled that Prudential apparently acquiesced in Judge Rigtrup's rendering a decision by failing to move for his disqualification until thirty-nine days after his ruling.[14] We concluded that Prudential's acquiescence was evidence that it did not

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[9] *Madsen v. Prudential Fed. Sav. & Loan Ass'n*, 767 P.2d 538, 541 (Utah 1988).

[10] *Id.* at 539-40.

[11] *Id.* at 541.

[12] 767 P.2d 538 (Utah 1988).

[13] *Id.* at 543.

[14] *Id.* at 543-44.

believe that Judge Rigtrup should recuse himself.[15] Further, we noted that although Judge Rigtrup had personal knowledge of some of the disputed facts and had a financial interest in the outcome of the case, the presiding judge expressly found no actual bias.[16]

¶ 13 Following the remand, Judge Rigtrup made a number of rulings, some of which the parties challenge in this appeal. First, he defined the class consistent with the Madsens' complaint as borrowers who had purchased a "single[-]family, owner-occupied, primary residence." This ruling excluded from the class borrowers who financed second homes, commercial properties, and multiplexes. Second, he ruled that the four-year statute of limitations in Utah Code section 78-12-25(3), "for relief not otherwise provided for by law," applied to the case. Third, he ruled that the 1979 Interest on Mortgage Loan Accounts Act cut off damages as of 1979. Thus, he limited the Madsens to recovering for the period from 1971 to 1979. Fourth, he ruled that the Madsens were not entitled to prejudgment interest but that interest during the eight-year period would be compounded. Fifth, he appointed a special master to locate and define the class members and ascertain damages. The special master filed a final report on March 1, 2002, concluding that there were 9,547 class members, who were owed an average of $105.18, resulting in a total

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[15] *Id.*

[16] *Id.* at 544.

judgment of $1,004,153. The trial court, now presided over by Judge L.A. Dever, entered a judgment for that amount.

¶ 14 The Madsens appeal, and WAMU cross-appeals. Each asserts multiple errors. The Madsens assert that the district court erred by

(1) applying a four-year statute of limitations rather than applying a six-year statute of limitations or holding that no limitations period applied;[17]

(2) ruling that the 1979 Interest on Mortgage Loan Accounts Act cut off damages after 1979;

(3) failing to award prejudgment interest covering the period from 1979 to the judgment;

(4) narrowing the class to include only borrowers who financed owner-occupied single-family homes, which excluded

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[17] Utah Code section 78B-2-307 (Supp.2008), which the court applied, provides that "[a]n action may be brought within four years . . . for relief not otherwise provided for by law." The Madsens argue that the court should have applied the former section 78-12-34 (now repealed), which provided that "actions [may be] brought, to recover money or other property deposited with any bank, trust company or savings and loan corporation, association or society, [without] limitation," or, in the alternative, section 78-12-25(2) (now amended), which provided a six-year statute of limitations for actions founded "upon any contract, obligation, or [for] liability founded upon an instrument in writing."

borrowers who financed duplexes, second homes, and commercial properties; and

(5) failing to disqualify the special master because he held ex parte meetings with WAMU and relied heavily on the work of WAMU employees.

¶ 15 The Madsens further argue that we should simplify the accounting of the profits earned and end the case by ordering the district court to use the passbook savings rate instead of continuing the case with a newly appointed special master.

¶ 16 WAMU cross-appeals, asserting that the district court

(1) erred as a matter of law by not granting summary judgment on the basis that federal law as codified in 12 C.F.R. § 545.6-11(c) preempts the Madsens' state law claims;[18]

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[18] WAMU preserved its federal preemption argument by making the argument to the district court both before and after *Madsen I* and to the federal district court. However, WAMU's brief in this appeal did not include a citation to the record showing that it had preserved this issue as required by our rule 24(a)(5) of the Utah Rules of Appellate Procedure. While we decline to sanction WAMU under rule 24(k), we warn future litigants that compliance with our briefing requirements is not discretionary, and litigants who fail to comply take the risk that we may disregard or strike briefs or arguments. *See, e.g., Peters v. Pine Meadow Ranch Home Ass'n*, 2007 UT 2, ¶ 23, 151 P.3d 962. We decline to disregard WAMU's preemption argument

(Continued on following page)

(2) erred by excluding evidence of a "special agreement" between the parties that no interest be paid on the pledged funds;

(3) erred in certifying the class under rule 23(b)(1)(A) of the Utah Rules of Civil Procedure; and

(4) erred in awarding compound interest during the 1971 to 1979 accounting period.

¶ 17 We have jurisdiction pursuant to Utah Code section 78A-3-102(3)(j) (Supp.2008).

ANALYSIS

¶ 18 In this opinion, we will first discuss the law of preemption generally. Then, we will discuss WAMU's argument that federal law preempts the Madsens' claim. We will also address the Madsens' contention that both this court and the Tenth Circuit have already decided the preemption question in the Madsens' favor in *Madsen I* and *Madsen II,* respectively. Because we hold that federal regulations preempt the Madsens' claim, it is unnecessary to reach the other issues on appeal and cross-appeal.

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because, despite WAMU's oversight in this regard, it is clear that WAMU preserved the federal preemption argument and otherwise fully complied with the briefing requirements found in rule 24.

I. FEDERAL LAW PREEMPTS CONFLICTING STATE LAW

¶ 19 Whether federal law preempts a state law cause of action is a question of law.[19] We review questions of law for correctness, giving no deference to the ruling of the court below.[20] Under the Supremacy Clause of the United States Constitution,[21] federal law preempts state law "where it regulates conduct in a field that Congress intended the Federal Government to occupy exclusively" or "to the extent that it actually conflicts with federal law."[22] In either case, it does not matter whether the state law is statutory or common law or whether the federal law is a federal regulation or statute of Congress.[23]

¶ 20 In this case, WAMU has argued that the Madsens' state law accounting claim, which requires WAMU to pay profits earned on the Madsens' pledged funds, conflicts with federal law as codified in 12 C.F.R. § 545.6-11(c). WAMU contends that under this regulation and other federal laws, it has no obligation

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[19] *See Dep't of Human Servs. v. Hughes*, 2007 UT 30, ¶ 15, 156 P.3d 820; *see also Retherford v. AT & T Commc'ns*, 844 P.2d 949, 958-59 (Utah 1992).

[20] *R.A. McKell Excavating, Inc. v. Wells Fargo Bank, N.A.*, 2004 UT 48, ¶ 7, 100 P.3d 1159.

[21] U.S. Const. art. VI, cl. 2.

[22] *English v. General Elec. Co.*, 496 U.S. 72, 79, 110 S.Ct. 2270, 110 L.Ed.2d 65 (1990).

[23] *See Free v. Bland*, 369 U.S. 663, 667-68, 82 S.Ct. 1089, 8 L.Ed.2d 180 (1962).

to pay interest or earnings on such accounts. If, under federal law, WAMU has no obligation to pay interest or earnings on the Madsens' pledged funds, federal law conflicts with, and therefore preempts, the Madsens' state law accounting claim.

II. UNDER FEDERAL REGULATIONS IN EFFECT AT THE TIME OF THE CONTRACT, PRUDENTIAL HAD NO OBLIGATION TO PAY INTEREST ON RESERVE ACCOUNTS

¶ 21 WAMU argues that 12 C.F.R. § 545.6-11(c), which exempts federal savings and loan associations from paying interest under certain circumstances, preempts any state law under which the Madsens might recover. That section reads as follows:

> A Federal association which makes a loan on or after June 16, 1975, on the security of a single-family dwelling occupied or to be occupied by the borrower (except such a loan for which a bona fide commitment was made before that date) shall pay interest on any escrow account maintained in connection with such a loan (1) if there is in effect a specific statutory provision or provisions of the State in which such dwelling is located by or under which the State-chartered savings and loan associations, mutual savings banks and similar institutions are generally required to pay interest on such escrow accounts, and (2) at not less than the rate required to be paid by such State-chartered institutions but not to exceed the rate being paid by the Federal

> association on its regular accounts (as defined by Section 526.1 of this chapter). Except as provided by contract, a Federal association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph.[24]

¶ 22 Under this regulation, Prudential had no obligation to pay interest to the Madsens absent a state statute or contractual obligation to the contrary. The Madsens' accounting claim is not founded on a contract or statute. By its express terms, however, the regulation applies only prospectively to loans made after June 16, 1975. It does not apply to the Madsens' loan, which Prudential made in 1964. But WAMU argues that § 545.6-11(c) did not alter the federal law applicable to the loans made before 1975. Rather, WAMU contends, the 1975 change merely reaffirmed the impact of two existing regulations, which also provide that Prudential had no obligation to pay interest to the Madsens.[25]

¶ 23 WAMU is correct. Two regulations predating the Madsens' loan, 12 C.F.R. §§ 544.1 and 541.5, directly conflict with the Madsens' state law cause of action. Both regulations became part of the federal register in 1958 and thus apply to the Madsens' 1964

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[24] 12 C.F.R. § 545.6-11(c) (1976).

[25] The Home Owners' Loan Act of 1933 created the Federal Home Loan Bank Board, which promulgated regulations governing the savings and loan industry beginning in 1933.

loans.[26] Section 544.1 provides that a federal home loan association such as Prudential "is not required to distribute earnings on short-term savings accounts."[27] Section 541.5 defines short-term savings accounts to include "a savings account in a Federal association established for the purpose of accumulating funds to pay taxes or insurance premiums, or both, in connection with a loan on the security of a lien on real estate."[28] The Madsens' account held by Prudential fits this definition precisely. Therefore, the account is subject to section 544.1, which explicitly provides that lenders who hold such accounts have no obligation to pay interest or earnings absent an agreement or state statute. The regulations directly conflict with the Madsens' state law claim. Federal law, therefore, preempts the Madsens' state law claim for interest on their account.

III. NEITHER THIS COURT NOR THE TENTH CIRCUIT HAS YET RULED ON THE MERITS OF THE FEDERAL PREEMPTION ISSUE

¶ 24 The Madsens do not make any attempt to counter WAMU's federal preemption argument on the merits. Instead, their argument on appeal consists entirely of an assertion that the federal preemption issue has already been decided by this court in

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[26] 23 C.F.R. § 9893 (1958).

[27] 12 C.F.R. § 544.1 (1975).

[28] 12 C.F.R. § 541.5 (1975).

Madsen I and by the Tenth Circuit in *Madsen II*. But our opinion in *Madsen I* did not address, much less decide, the issue of federal preemption. And in *Madsen II*, the Tenth Circuit dismissed the case purely for lack of federal jurisdiction. As we did not rule on the merits of WAMU's federal preemption argument in *Madsen I*, and as the Tenth Circuit dismissed the case for lack of jurisdiction without reaching the merits in *Madsen II*, we now address for the first time the merits of WAMU's federal preemption argument.

A. *We Did Not Rule on the Merits of Federal Preemption in* Madsen I

¶ 25 The issue of preemption was not before us in *Madsen I*.[29] The district court had ruled that neither the contract nor the principles of pledge gave rise to a claim upon which relief could be granted. The district court did not rule on the issue of preemption. Accordingly, neither party appealed the issue of federal preemption. Our decision in *Madsen I* focused exclusively on whether the Madsens' budget payments satisfied the elements of a common law pledge.[30] We reversed the district court's ruling, holding that the budget payments met the elements of a common law pledge because there was "a debt or obligation, a transfer of property to the pledgee, to be held as

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[29] 558 P.2d 1337 (Utah 1977).

[30] *Id.*

security and, if necessary, to be used to assure performance of the obligation."[31] The decision did not include a single reference to any federal law, much less a resolution of whether federal law preempts the Madsens' accounting claim.

¶ 26 The Madsens' argue that, although they did not appeal the issue of preemption and neither our opinion nor the district court's grant of summary judgment addressed preemption, "Prudential's federal theory has already been presented to the Utah Supreme Court" and that "[i]f 12 C.F.R. § 545.6-11(c) destroyed Madsen's [sic] cause of action, the Utah Supreme Court would have been forced to affirm the trial court's dismissal over thirty years ago." This assertion is contrary to our well-established precedent that "an appellate court *may* affirm the judgment appealed from 'if it is sustainable on any legal ground or theory apparent on the record.'"[32] When reviewing a decision made on one ground, we have the *discretion* to affirm the judgment on an alternative ground if it is apparent in the record. But that cannot mean, as the Madsens' contend here, that our declining to rule on an alternative ground can be construed as a ruling on the merits of the alternative ground, particularly when the alternative ground has not been argued by either party to the appeal. In fact,

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[31] *Id.* at 1339.

[32] *Dipoma v. McPhie*, 2001 UT 61, ¶ 18, 29 P.3d 1225 (emphasis added) (quoting *Limb v. Federated Milk Producers Ass'n*, 23 Utah 2d 222, 461 P.2d 290, 293 n. 2 (1969)).

we frequently decline to rule on an issue when it has not been fully briefed by the parties because full briefing allows this court to carefully consider fully developed and supported arguments.[33] The decision not to reach an alternative ground is certainly not binding on the court below, particularly when the parties did not argue the issue and this court's decision does not include so much as a single reference to the issue now supposedly foreclosed.

¶ 27 In support of their argument that we have already ruled on the issue of preemption, the Madsens assert that Prudential made the federal preemption argument in its briefs. In fact, Prudential's appellate brief in *Madsen I* cited federal banking regulations, including 12 C.F.R. § 545.6-11(c) in support of its policy argument against applying the law of pledge. But Prudential did not mention the law of federal preemption. The Madsens' briefs in that appeal likewise did not argue preemption. Thus the Madsens are incorrect in arguing that we have already decided the preemption issue. Having determined that we did not decide the issue in *Madsen I*, we now address the Madsens' contention that the Tenth Circuit decided the preemption issue in *Madsen II*.

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[33] *See, e.g., Pearson v. Pearson*, 2008 UT 24, ¶ 10 n. 8, 182 P.3d 353 (declining to apply the Utah Uniform Parentage Act to a child custody dispute because the parties did not argue or brief the issue under that law).

B. The Tenth Circuit Did Not Rule on the Merits of Federal Preemption In Madsen II

¶ 28 In *Madsen II,* the Tenth Circuit ruled on the Madsens' appeal from the federal district court, which had granted summary judgment in favor of Prudential on the basis of preemption:

> Under the federal preemption doctrine, Madsens have no claim against Prudential for interest on their escrow account. 12 C.F.R. § 545.6-11(c) clearly precludes the relief the Madsens are seeking. . . . More importantly, the regulation cited above does not appear to alter the federal law applicable to loans made before June 16, 1975, but instead appears to reaffirm the impact of 12 C.F.R. §§ 544.1 ("association is not required to distribute earnings on short-term savings accounts") and 541.5 (defining short-term savings account as including mortgage loan escrow accounts for taxes and insurance).[34]

The Madsens argued that the federal court lacked jurisdiction and appealed to the Tenth Circuit.[35] The issue on appeal was whether the federal court had federal question jurisdiction, specifically whether the suit arose under the Constitution or laws of the United States.[36] The Tenth Circuit held that federal jurisdiction existed only if the "federal right or

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[34] 635 F.2d 797, 800 (10th Cir.1980).

[35] *Id.*

[36] *Id.*

immunity [is] an essential element of the plaintiff's cause of action, and that the federal controversy must be 'disclosed on the face of the complaint, unaided by the answer or by the petition for removal.'"[37] It went on to hold that "[b]ecause the Madsens have predicated their suit upon rights created under state law, the fact that federal regulations may create a defense to recovery on such a claim is immaterial to a finding of federal question jurisdiction."[38]

¶ 29 Although the Tenth Circuit explicitly ruled on jurisdictional grounds, the Madsens argue that the following language in the Tenth Circuit's opinion constitutes a decision on the merits of the preemption argument:

> Here, it is vigorously argued that application of state law would create a significant conflict because federal policy requires uniform nationwide standards for the handling of escrow accounts by federal savings and loan associations. This argument founders on the very language of the regulation cited to support it. Section 545.6-11(c) provides that a federal savings and loan association shall pay interest on escrow accounts if a state statute requires such payments to be made by state-chartered institutions, or if payments are required by contract. The

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[37] *Id.* (quoting *Gully v. First Nat'l Bank*, 299 U.S. 109, 113, 57 S.Ct. 96, 81 L.Ed. 70 (1936)).

[38] *Id.* at 801.

> regulation expressly anticipates that the obligation of a federal institution to pay interest on escrow accounts not only will vary from state to state, but from contract to contract.
>
> . . .
>
> Given the absence of a significant conflict between the federal policy expressed in section 545.6-11(c) and the use of state law, we hold that state law is applicable in determining whether Prudential *contracted to pay interest* on the Madsens' escrow account.[39]

¶ 30 This, the Madsens argue, is the Tenth Circuit's pronouncement that the federal regulation does not conflict with their claim for interest, and thus federal law does not preempt their state law claim.

¶ 31 The Madsens are incorrect. The discussion cited above is presented in response to Prudential's argument that the controversy required the court to apply federal common law in determining whether the parties had entered into a contract for the payment of interest. A controversy that requires the application of federal common law necessarily arises under the laws of the United States. But federal courts only apply federal common law to cases in which there is "a significant conflict between some

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[39] *Id.* at 802-03 (emphasis added).

federal policy or interest and the use of state law."[40] The passage cited by the Madsens is the Tenth Circuit's acknowledgment that under the explicit terms of 21 C.F.R. § 545.6-11(c), lenders' interest obligations could be varied by contract between private parties. The question of whether such a private contract had been created is, as the Tenth Circuit concluded, governed by state law. Interest obligations that varied from state to state or from contract to contract would not disrupt a federal scheme requiring uniformity.

¶ 32 In this case, however, the Madsens have not claimed that a provision in the contract obligated Prudential to pay interest. Indeed, there is no such provision. Moreover, they concede that there is no applicable state statute. So while the federal regulation explicitly permits the interest obligation to vary by private contract or by state statute, in this case we have neither. And in the absence of a contract or statute, the regulation is clear that Prudential had no obligation to pay interest. The mere fact that the Tenth Circuit acknowledged that under the explicit terms of the regulation, the interest obligation may be established by private contract or statute in no way changes the fact that absent either, Prudential had no obligation to pay interest on the budget payment accounts.

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[40] *Wallis v. Pan Am. Petroleum Corp.*, 384 U.S. 63, 68, 86 S.Ct. 1301, 16 L.Ed.2d 369 (1966).

¶ 33 Thus the Madsens are incorrect in arguing that this court or the Tenth Circuit has already decided the preemption issue, and it is appropriate that we resolve the issue in this appeal. For the reasons discussed in section II, we reverse the district court's ruling, hold that federal law preempts the Madsens' accounting claim, and remand with instructions to enter summary judgment in favor of WAMU. Because we decide that federal law preempts the Madsens' claim, it is unnecessary to reach the other issues in this appeal.

CONCLUSION

¶ 34 We conclude that federal law preempts the Madsens' claim for profits earned on pledged funds in reserve accounts maintained by Prudential in connection with their real estate mortgage. Because federal law preempts the Madsens' cause of action, it is unnecessary to reach the other issues presented by the parties in this appeal. We reverse and remand with instructions to enter summary judgment in favor of WAMU.

¶ 35 Chief Justice DURHAM, Justice PARRISH, Judge GREENWOOD, and Judge WESTFALL concur in Associate Chief Justice DURRANT'S opinion.

¶ 36 Having disqualified himself, Justice WILKINS does not participate herein; District Court Judge G. MICHAEL WESTFALL sat.

¶ 37 Justice NEHRING does not participate herein; Court of Appeals Judge PAMELA T. GREENWOOD sat.

APPENDIX B

IN THE THIRD JUDICIAL DISTRICT COURT
IN AND FOR SALT LAKE COUNTY,
STATE OF UTAH

RICHARD MADSEN and NANCY MADSEN, his wife, for themselves and all others similarly situated, Plaintiff, v. WASHINGTON MUTUAL BANK fsb (successor to PRUDENTIAL FEDERAL SAVINGS and LOAN ASSOCIATION), Defendant.	**FINAL JUDGMENT** Civil No. C79-8404 [#75026073] Honorable L. A. Dever (Entered Jun. 1, 2006)

It is hereby ordered, adjudged, and decreed that:

1. Judgment is entered against defendant Washington Mutual Bank fsb, successor to Prudential Federal Savings and Loan Association in the amount of $1,004,153 as the total lump sum damages and in favor of Nancy Madsen, in her capacity as representative of a certified class of persons, similarly situated, consisting of the borrowers on the 9,547 loans identified by the Special Master comprising a class defined as borrowers (i) whose loan include a trust deed containing the pledge language as in the Madsens'

Trust Deed, as identified by the Special Master; (ii) who had any funds in escrow reserve budget accounts between March 3, 1971 and June 30, 1979; (iii) whose loan was for a single-family, owner-occupied, residential primary residence; (iv) whose loan originated in Utah; and (v) whose mailing address and property address are identical on the Mortgage Loan Master Reference Card, thereby establishing "primary residence." The actual names of class members can be provided to the appellate court by supplemental filing if so desired or requested by the appellate court.

2. The amount of the foregoing aggregate judgment to be received by class members for each loan within the class is the cumulative net earnings on the average escrow balance for that class member's loan, compounded for the period March 3, 1971 to June 30, 1979, arrived at by applying the following "net yield" for each year:

1971	3.17%
1972	2.97%
1973	6.01%
1974	6.76%
1975	4.59%
1976	3.20%
1977	3.95%
1978	5.94%
1979	8.89%

less attorneys' fees awarded to plaintiffs' counsel in the amount of 33.3% of the foregoing.

3. Defendant Washington Mutual Bank fsb shall pay post-judgment interest, at the rate set forth

in Utah Code Ann. § 15-1-4, from the date of this Judgment, until the amount of the aggregate is deposited in court, in cash or bond.

4. Defendant Washington Mutual Bank fsb shall pay plaintiffs' costs to the extent required by Utah Rule of Civil Procedure 54, and as determined by the Court, in the amount of _____.

DATED May 31, 2006.

BY THE COURT:

/s/ L A Dever
Honorable L.A. Dever

[SEAL]

CERTIFICATE OF SERVICE

I certify that on June 19th, 2005, a true and correct copy of the foregoing proposed **FINAL JUDGMENT** was hand-delivered to the following:

Robert J. DeBry
DEBRY & ASSOCIATES
4252 South 700 East
Salt Lake City, Utah 84107

/s/ Linda Lilyquist

APPENDIX C

ROBERT J. DEBRY – A0849
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Salt Lake City, Utah 84107
Telephone: (801) 262-8915

IN THE DISTRICT COURT OF THE
THIRD JUDICIAL DISTRICT IN AND FOR
SALT LAKE COUNTY, STATE OF UTAH

RICHARD MADSEN and NANCY MADSEN, his wife, for themselves and all others similarly situated, Plaintiffs, vs. PRUDENTIAL FEDERAL SAVINGS AND LOAN ASSOCIATION, for itself and all others similarly situated, Defendants.	FINDINGS OF FACT AND CONCLUSIONS OF LAW Civil No. 226073 JUDGE KENNETH RIGTRUP (Filed Mar. 22, 1990)

PREAMBLE

On September 4, 5, and 6, 1985, this case was tried to the Court without a jury. Plaintiff was represented by Robert J. DeBry. Defendant was represented by Joseph Palmer and Reid E. Lewis.

Although this is a class action, the Court has ordered the parties to present evidence during this stage of the proceedings only for Madsen individually.

At the outset of the trial, Madsen made a motion to bifurcate, and demanded a jury to hear evidence on a Statute of Limitations issue: viz. when Madsen knew or should have known of Prudential's alleged misconduct (Motion to Bifurcate, August 27, 1985). Prudential made a Motion to Strike the Jury Demand (August 30, 1985). The Court ruled that the discovery rule would not toll the statute of limitations and that the request for a jury trial was therefore denied. In making its ruling, the court announced that:

(a) When the Madsens entered the contract, they got a copy of it and they had an opportunity to read it before they signed it.

(b) The contract made no provision about interest specifically.

(c) The Madsens knew or should have known about the absence of interest provisions in the contract.

(d) The Madsens could have ascertained Prudential's financial circumstances if profits or interest had been of any concern to them.

(e) The Madsens were members or shareholders of Prudential and, as such, they were entitled to examine business records and books and obtain a profit and loss statement and to inquire into such documents.

Prudential contended that there were 24 additional issues in the case. Prudential timely reserved the following issues in this case:

(a) Whether the parties intended earnings to be paid or whether, considering all circumstances, including their conduct, the benefit the Madsens received, and the industry custom and practice, they intended a special agreement that earnings not be paid.

(b) Whether the parties intended a true pledge relationship or a debtor-creditor relationship.

(c) Whether the budget funds are pledged property or a commingled, fungible cash deposit.

(d) Whether Prudential was unjustly enriched by use of the budget funds.

(e) Whether payment of earnings on the Madsens' budget funds has been preempted by federal law and regulations of the Federal Home Loan Bank Board as a matter of fact and of law, since 1964.

(f) Whether the Madsens have waived their claims, or they are barred by estoppel or laches from asserting them.

(g) Whether the Madsens' budget account is a "short term savings account" within the meaning of 12 C.F.R. § 541.5.

Prudential made the following offer of proof to support their affirmative defenses:

(a) Affidavit of Edwin Calvert.

(b) Affidavit of Gibbs Marsh.

(c) Prudential's Answers to Interrogatories.

(d) Prudential's Charter (1977).

(e) Deposition of Arthur Liebold.

(f) Deposition of plaintiff Madsen.

(g) Documents produced by the Federal Home Loan Bank Board.

(h) Prudential's annual reports.

(i) Briefs on appeal.

(j) Unspecified testimony of Mr. Adams – an auditor of Prudential Federal.

The offer of proof was received and denied. Rather, the Court limited the scope of this trial to whether Prudential has earned a profit from the use of the pledged funds, and if so, for an accounting of those profits. (Compare, *Order,* dated September 3, 1985.)

With the case in this procedural posture, and after hearing evidence of the parties, the Court enters the following findings of fact and conclusions of law:

FINDINGS OF FACT

1. Madsen entered into a trust deed contract with Prudential on September 24, 1964.

2. Pursuant to this contract, Madsen was required to make monthly advance payments for anticipated taxes and insurance premiums. These advance payments were known as "budget payments."

3. Payments were prompted by a monthly request for payment, or a bill from Prudential to Madsen.

4. Madsen tendered a single check for his monthly payment. This single check included principle, interest and "budget payment". Madsen submitted this monthly payment together with a copy of the monthly bill or the billing stub. Prudential maintained separate accounting records to credit Madsen for payment of principle, interest and "budget" funds.

5. Upon receiving each monthly payment, Prudential immediately deposited the entire check into its general operating account.

6. Payments for Madsen's taxes and insurance premiums were taken out of this general account as needed periodically. The property taxes and insurance premiums were paid by Prudential on an annual basis. Prudential made annual reports to Madsen about the specific allocation and payment of Madsen budget funds for taxes and insurance premiums.

7. Prudential also used this general operating account for routine business expenses such as office lease payments, salaries, office machines, etc.

8. Prudential invests most surplus funds from the general operating account in short term investments such as U.S. Treasury Bills, U.S. Treasury Notes, Certificates of Deposit, and certain Federal Agency obligations. However, Prudential also uses the same general operating account to make some longer term investments at higher yields. Prudential earns a profit on all of those investments.

9. It is possible, by using Prudential's financial records, to determine the amount of income which Prudential has received by investing surplus funds from the general operating account. The Court has also determined that a portion of that income is attributable to Madsen's "budget" payments. The income attributable to Madsen's "budget" payments is set forth in Exhibit A attached.

10. In computing that income (paragraphs 8 and 9 above), the Court has assumed that the excess funds were invested in short term Treasury Bills because such Treasury Bills would be liquid and readily available to pay for Madsen's taxes and insurance when due. In fact, in addition to Treasury Bill investments, Prudential made other investments at higher yields.

11. Prudential undergoes a number of procedural steps in order to process tax and insurance bills, and to pay those amounts on behalf of Madsen.

However, the Court specifically finds that Prudential would be performing many of those same steps with or without the "budget" payments. For example, Prudential sends a monthly statement to Madsen. However, Prudential would send that same statement to request the monthly mortgage payment even if there were no "budget" payments.

12. Based upon the evidence in the record, the Court has found the costs which Prudential incurred in handling and managing the "budget" funds, including the cost of processing tax and insurance payments, as included in Exhibit A.

13. The difference between income and expenses on Exhibit A represents profits or earnings which Prudential has realized by its use and investment of Madsen's "budget" funds.

14. The Court finds it appropriate under the facts of this case to compound on an annual basis. The Court finds that Prudential must disgorge these compounded profits in order to make Madsen whole. The compounded earnings are included in Exhibit A.

15. For the period of March 3, 1971 to June 30, 1979, Prudential's earnings or profits realized by using Madsen's "budget" payments amount to $109.43. That amount is increased to $134.70 by compounding on an annual basis up to June 30, 1979.

16. The combined table of the Court's findings on profits or earnings is attached as Exhibit A.

17. It was not disputed that on or about July 25, 1979, Madsens received a letter from Prudential reproduced at Exhibit B of these findings (or, Exhibit A-1 of Madsen's Third Amended Complaint). Exhibit B is the letter that Prudential mailed out based upon *Utah Code Ann.* § 7-17-4.

18. It was not disputed that Madsens responded to Prudential's letter of July 25, 1979 in a letter dated September 4, 1979, reproduced at Exhibit C of these findings (or, Exhibit B of the Third Amended Complaint).

19. It was not disputed that Madsen did not withdraw his "budget account" from Prudential after receiving Prudential's letter of July 25, 1979.

CONCLUSIONS OF LAW

1. The law of this case was set by the Utah Supreme Court in the case of *Madsen v. Prudential Federal Savings & Loan Assn.*, 558 P.2d 1337 (Utah 1977), and by the Memorandum Decision of the Honorable Bryant Croft dated June 14, 1977.

2. Specifically, the law of the case is that the "budget" payments made by Madsen for taxes and insurance constitute a common law pledge. If Prudential has realized any profits or earnings from the use of the pledged funds, Prudential must disgorge those profits to Madsen.

3. This case is an action for an accounting in equity.

4. The applicable statute of limitations for this case is four years, pursuant to § 78-12-25(2), "An action for relief not otherwise provided for by Law." The complaint was filed on March 3, 1975. Therefore, the damage period shall begin on March 3, 1971.

5. Damages terminate on June 30, 1979 by reason of *Utah Code Ann.* § 7-17-4.

6. *Utah Code Ann.* § 7-17-4, is not an unconstitutional impairment of contract under U.S. Constitution Article I, Section 10 or Utah Constitution Article I, Section 18. The notice sent by Prudential to Madsen (pursuant to *Utah Code Ann.* § 7-17-4) does not offend the due process requirements of the U.S. Constitution or the Utah State Constitution since Madsen was represented by counsel who would advise him as to the legal effect of *Utah Code Ann.* § 7-17-4. Furthermore, neither § 7-17-4 nor the said notice take vested rights from Madsen in violation of Utah Constitution Article I, Section 7, or the Fourteenth Amendment to the United States Constitution.

7. The doctrine which would toll the statute of limitations until the injured party discovers or reasonably should have discovered the harmful conduct is not applicable to this case (see Preamble).

8. The statute of limitations is not tolled by reason of Madsen's claim that a continuing illegal business practice should toll the statute.

9. The "budget" account is not a "bank deposit" within the meaning of *Utah Code Ann.* § 78-12-34.

10. Prudential should be ordered to pay to Madsen the sum of $134.70 for profits or earnings Prudential has realized by using Madsen's "budget" payments for the period of March 3, 1971 to June 30, 1979.

11. Madsen is entitled to his costs of action.

12. All class issues are reserved for further proceedings.

13. Plaintiffs shall have simple interest at the annual rate of 10% on the damages awarded to them in the Court's ruling of September 6, 1985, calculated from that date to the entry of judgment. Plaintiffs shall not be allowed interest for any time prior to trial, for the reasons that the damages were not calculable before trial, that damage calculation at trial was subject to divergent evidence and viewpoints, especially between the parties' expert witnesses, that damages required a determination by the Court and that the Court was required to select one method of calculation from among several alternatives presented by the experts.

DATED this 22nd day of March, 1990.

BY THE COURT:

By: /s/ Kenneth Rigtrup
HONORABLE KENNETH RIGTRUP

Approved as to Form:

/s/ Robert J. Debry
ROBERT J. DEBRY

Approved as to Form:

/s/ Joe J. Palmer
JOSEPH J. PALMER
REID LEWIS

CERTIFICATE OF MAILING

I certify that on the 21 day of March, 1990, I mailed a true and correct copy of the foregoing PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW, (Madsen v. Prudential), U.S. Mail, postage prepaid, to the following:

Joseph J. Palmer
Reid E. Lewis
MOYLE & DRAPER, P.C.
600 Deseret Plaza
Salt Lake City, Utah 84111-1901

/s/ Kathy Palmer

R. D. MADSEN

SCHEDULE 7A

AVERAGE ESCROW BALANCE
AND LOST INCOME AT NET U.S. T-BILL YIELDS

March 3, 1971 to June 30 1979

Year	Average Escrow Balance	Average T-Bill Yield	Average Expense Rate On Escrow Funds	Net Yield	Net Earnings On Escrow Funds	Cumulative Net Earnings Compounded
1971	$226.70	4.33%	1.16%	3.17%	$5.97	$5.97
1972	$284.94	4.07%	1.10%	2.97%	$8.46	$15.04
1973	$157.83	7.03%	1.02%	6.01%	$9.49	$25.72
1974	$219.72	7.84%	1.00%	6.76%	$14.85	$42.56
1975	$335.73	5.80%	1.21%	4.59%	$15.41	$60.99
1976	$225.06	4.98%	1.78%	3.20%	$7.20	$72.06
1977	$318.28	5.27%	1.32%	3.95%	$12.57	$89.34
1978	$402.81	7.19%	1.25%	5.94%	$23.93	$119.34
1979	$259.84	10.07%	1.18%	8.89%	$11.55	$134.70
			TOTALS;		$109.43	$134.70

C13

PRUDENTIAL FEDERAL SAVINGS

July 25, 1979

NOTICE TO HOME OWNERS

RESERVE ACCOUNTS FOR PAYMENT OF TAXES AND INSURANCE

As of July 1 1979, Prudential Federal Savings will no longer require a reserve account in conjunction with your mortgage loan for the payment of real estate property taxes, insurance premiums, or other charges. You may now choose one of the following two options:

A. You may continue your monthly payment as is now provided for in your loan documents to be deposited in a noninterest bearing reserve account. We will continue to provide you the service of paying your property taxes and/or insurance premiums at no cost as they become due; or,

B. You may elect to assume the legal responsibility for the payment of these assessments and pay your own real estate property taxes, insurance premiums and other charges as they become due.

If you choose Option A, no response is necessary. We will continue to provide the services of paying these assessments without cost to you. If you choose Option B, the enclosed card must be signed and returned to our office by September 1, 1979. Please send this card to:

Prudential Federal Savings and
Loan Association
P.O. Box 15500
Salt Lake City, Utah 84115

Attention: Mortgage Loan Servicing

Upon receipt of the card indicating that you wish to pay your own taxes, insurance and other charges on a direct basis, we will return to you the present balance in your reserve account and adjust your monthly payment accordingly.

While Prudential is governed by Federal and not State Law in matters dealing with the terms of a loan contract, the options as set forth herein are consistent with the provisions of Utah law.

Enclosure

(1) Option Card

September 4, 1979

CERTIFIED MAIL

Prudential Federal Savings & Loan Association
115 South Main Street
Salt Lake City, Utah 84111

RE: Richard and Nancy Madsen
Loan No. 335-018511-0

Gentlemen:

Mr. and Mrs. Madsen have consulted this office in connection with your letter of July 25, 1979 entitled, *Notice to Homeowners – Reserve Accounts for Payments of Taxes and Insurance.*

It appears that your letter is in violation of the express provisions of the *Interest on Mortgage Loan Reserve Accounts Act*, § 7-17-1, *et seq.*, Utah Code Ann. (1953). Specifically, your letter has claimed protection under § 7-17-4 Utah Code Ann. (1953); however, § 7-17-4 is clearly not applicable to the Madsen contract. That section provides in part:

> (1) A lender not requiring the establishment and maintenance of a reserve account shall offer the borrower the following options:

We have examined the Madsen contract. As you know, the contract contains a provision requiring the Madsens to make monthly payments into the Reserve Account. We are told by the Madsens that they had no choice in the matter. The contract was presented to them on a "take it or leave it" basis. In short,

Prudential has already "required" the Madsens to pay into the reserve account, and that requirement has been reduced to a written agreement. That requirement will, of course, continue to exist for the life of the contract. Thus it seems fair to conclude that the existing contract constitutes a continuing requirement.

We are not aware of any doctrine by which Prudential can now "unrequire" a reserve account. Stated in other words, Prudential cannot unilaterally change the written contract. Nor can the legislature change the written contract.

This analysis is confirmed by the use of the word *and* in the first sentence of § 7-17-4. Note that the word *and* is in the conjunctive. In other words, Prudential is entitled to the protection of § 7-17-4 only where both conditions exist conjunctively:

> First, the lender does not require the establishment of a reserve account,
>
> *and*
>
> second, the lender does not require the maintenance of a reserve account.

Prudential can never satisfy both of these conditions on existing loans. Even if Prudential does not require the maintenance of a reserve account in future; Prudential has nonetheless already required such a reserve for the past several years. The reserve account has already been established. Thus Prudential can never satisfy the first condition of § 7-17-4.

On the other hand, § 7-17-3, Utah Code Ann. (1953), is drafted in the *disjunctive*:

> (1) Each lender requiring the establishment, *or* continuance of a reserve account in connection with an existing or future real estate loan shall pay interest on funds deposited in the account after June 30, 1979 of at least 4% simple interest per annum. . . .

Thus, Prudential would fall under § 7-17-3 if it had required the establishment of a reserve account *or* if Prudential required the continuance of a reserve account. Prudential has already required the establishment of the reserve account by contract. Thus, § 7-17-3 is satisfied. Since the statute is drafted in the *disjunctive*, it really makes no difference at all the Prudential may somehow discontinue that requirement in the future. Section 7-17-3 is satisfied simply because Prudential required the reserve account in the existing contract. It is not necessary that both conditions be satisfied.

This all boils down to a fairly simple scenario. Prudential has sent out a series of letters announcing that the *policy* of requiring a reserve account has been reversed. Prudential next claims that it is entitled to the protection of § 7-17-4 because it has no policy requiring a reserve account. The fallacy in all of this is that the requirement for a reserve account arises from a *contract* – not a *policy*. The *contract* continues to exist. It cannot be changed at the mere whim and caprice of Prudential. The *contract* constitutes a continuing requirement. Since Prudential's

contract requires the reserve account, the transaction falls under § 7-17-3.

In view of the foregoing, we are convinced that the Madsen contract does not fall under § 7-17-4. Thus, pursuant to § 7-17-8(2), Utah Code Ann. (1953), we herewith demand payment of interest pursuant to § 7-17-3, Utah Code Ann. (1953). If you fail to honor this demand, it is our intent to file suit pursuant to § 7-17-8(1), Utah Code Ann. (1953).

It is further apparent that Prudential has sent similar or identical notices to other borrowers. Therefore, pursuant to § 7-17-8(2), Utah Code Ann. (1953), we make this demand on behalf of the Madsens and all other borrowers of Prudential similarly situated.

Moreover, we are informed that every lending institution in Utah has sent letters in substance and effect identical to the Madsen letter. It is inconceivable that all of these lending institutions could misread the simple language of the statute. Rather, we conclude that this parallel conduct is the result of a conspiracy by Utah Lending institutions to circumvent the requirements of § 7-17-3. By reason of such industry-wide practice and conspiratorial conduct, all Utah lending institutions are juridically related and subject to treatment as a defendant class under Rule 23 of the Utah Rules of Civil Procedure. Thus, by copy of this letter, we make demand under § 7-17-8(2) on behalf of all borrowers in the State of Utah who have received letters from any Utah lender in substance and effect similar to the Madsen letter.

APPENDIX D

767 P.2d 538

Supreme Court of Utah.
Richard MADSEN and Nancy Madsen, his wife,
for themselves and all others similarly situated,
Plaintiffs and Appellants,
v.
PRUDENTIAL FEDERAL SAVINGS AND LOAN
ASSOCIATION, Defendant and Appellee.
No. 860148.

Dec. 30, 1988.

Robert J. DeBry, Salt Lake City, for plaintiffs and appellants.

Joseph J. Palmer, Reid E. Lewis, Salt Lake City, for defendant and appellee.

STEWART, Justice:

Plaintiffs Richard and Nancy Madsen appeal a district court order entered by Judge Philip Fishler which disqualified Judge Kenneth Rigtrup after he had presided over a trial in this case and had orally announced his ruling but before he had entered formal findings of fact, conclusions of law, and final judgment. Judge Fishler ruled that Judge Rigtrup had no actual bias, but did have an appearance of bias and voided the trial and all prior orders entered by Judge Rigtrup in the case.

This appeal is yet another installment in the protracted history of this case, which started in 1975 and has already been before this Court once, *Madsen*

v. Prudential Fed. Sav. & Loan Ass'n, 558 P.2d 1337 (Utah 1977), and before a federal appellate court once, *Madsen v. Prudential Fed. Sav. & Loan Ass'n,* 635 F.2d 797 (10th Cir.1980), *cert. denied,* 451 U.S. 1018, 101 S.Ct. 3007, 69 L.Ed.2d 389 (1981). The facts which gave rise to this litigation are reported in detail in those opinions. 558 P.2d at 1338-39; 635 F.2d at 799-800.

Plaintiffs are representatives of a certified class of borrowers whose trust deeds with Prudential Federal Savings and Loan Association (hereafter "Prudential") contained language identical to that contained in the Madsens' trust deed. In 1984, this action was assigned to Third District Court Judge Kenneth Rigtrup who had been assigned to four other similar cases.[1] Prudential appeared as amicus curiae in each of the other actions.

The issue here was whether a financial institution which loaned money to the plaintiffs on a first

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[1] *Roger Hal Read and Elizabeth W. Read,* for themselves and all others similarly situated *v. American Equity Corporation,* for itself and all others similarly situated, district court No. C-244219 (filed August 11, 1977). *James W. Petty and Mary E. Petty,* for themselves and all others similarly situated *v. Western Savings and Loan Co.,* district court No. C-79-700 (dismissed July 19, 1983). *Russell R. Everill and Helen B. Everill,* for themselves and all others similarly situated *v. Western Savings and Loan Co.,* district court No. C-79-701 (dismissed July 19, 1983). *Ernest H. Dixon and Lori Ann P. Dixon,* for themselves and all others similarly situated *v. United Savings and Loan Ass'n,* district court No. C-79-1105 (filed February 16, 1979).

trust deed is obligated to pay interest to the plaintiffs on monthly budget payments for property taxes and insurance that are paid with the monthly mortgage payments. In a bench trial in September 1985, the Madsens and Prudential tried the limited issue of whether Prudential made any profit on the budget payments it collected from the Madsens. At the close of the trial, Judge Rigtrup ruled from the bench. Just prior to his ruling, the following exchange occurred between Judge Rigtrup and counsel for the parties:

> THE COURT: . . . I'll share the benefits of my decision with you at this point.
>
> . . . I'll expose my biases and my prejudices and be very frank with you.
>
> I think there are some substantial kinds of policy things that have really caused me great trouble and trauma. As I've indicated earlier, and no objection was interposed, I was a customer of Prudential Federal Savings & Loan Association and paid without default for 25 years at four and three-quarters per cent, . . . and I computed that out and I thought, why, those robbers, they are charging me twice what I'm borrowing from them, and that's unfair.
>
> As I get older and more sophisticated I –
>
> MR. PALMER [Attorney for Prudential]: Your Honor, I hate to interrupt, but I need to make the point that this is news to me, that you had been a customer of Prudential.

THE COURT: I indicated that on several occasions.

MR. PALMER: I beg the Court's pardon, but that is news to me. I don't recall that at all – if anybody else does – recall you telling me that, and I –

THE COURT: I indicated that in these earlier meetings that I had paid my loan off at some point, and I'd had a loan with Prudential Federal Savings.

MR. PALMER: Perhaps the Court is thinking of conferences with other counsel. The reason I make the point is –

THE COURT: My earlier conferences were not with the two of you in this case, they were with Mr. Billings, with Mr. Ashton, with you, with Mr. Giauque, Mr. McDonough, with respect to whoever he represents. It was Mr. Giauque or someone from that office. They were a corrective kind of a deal.

MR. PALMER: In any event, I stand to raise the point now that it is news to us. I believe it – I take it that the Court did not feel that it had any prejudice because of that.

THE COURT: No.

MR. PALMER: All right.

THE COURT: I have a recollection that somewhere along the line I did make that disclosure. I don't know how you could be part of the community and be a homeowner and not have borrowed from someone. And so

I think I make it very clear in one of those collective kinds of meetings that my loan had been with Prudential Federal.

At any rate, it's a fact, and it was something that I never tried to hide or have hid from anyone. So there's no sense of covering up. I guess if that creates error, it creates error. But so be it. I have a recollection that I did expose it, and whether you were there or Mr. Lewis or anyone else, I don't know. I did make the disclosure early on.

MR. DeBRY [Attorney for the Madsens]: I do recall some conversations, I think, off the record, of that effect, and I honestly don't recall who was present. But it was a comment that was made from time to time.

MR. PALMER: Could I inquire of the Court when the loan was paid off?

THE COURT: Probably two years ago. I'm not sure at what point in the discussions I indicated that, but I'm sure that in the presence of the collective group that I indicated that I had been a borrower of Prudential Federal Savings.

MR. PALMER: No prejudice arose in the Court's mind because of the fact that we collected a mortgage escrow from you?

THE COURT: No.

MR. PALMER: Okay. I can't do anything else but ask.

THE COURT: That's what I've been trying to tell you. That was the intention.

MR. PALMER: I make the point because I didn't want to go on and let the Court note –

THE COURT: I think I've made general comments throughout that I have cussed financial institutions, and customers do simply because they see inherent injustice about that. And my perspective today, after 23 years has passed, has become much, much different at the end of the 23 years. Far before that I could see the cost of money was markedly greater, and that I would be a damn fool to prepay. So I paid faithfully every month for 25 years, and not a day sooner or a day later. And I'm just commenting generally in terms of unjust or whatever. The tension is between that to be gained and that to be lost, I suppose, in my eyes. And I have a feeling that class actions are a form of champerty and maintenance in that the one that substantially gains is the lawyer or the expert. Mr. Madsen stands to gain little, except he has struck a blow for freedom, I suppose, in the form that the consumer has achieved balance.

Be seated, Mr. DeBry.

MR. DeBRY: I want to make an objection on the record. I really must.

THE COURT: Well, sit down.

MR. DeBRY: Before you give your decision, I must make a comment, because I know the

Court is being candid and this has been a long struggle, and Prudential says they are almost broke before this. And you say maybe DeBry will make some money, but I haven't yet. But I really must interpose an objection at this point. If the Court harbors this type of personal bias with respect to –

THE COURT: I'm just –

MR. DeBRY: – class actions.

THE COURT: I'm just telling you about the tension.

MR. DeBRY: I must object to the Court's sitting on this case if you have that kind of bias.

THE COURT: I'm just telling you why I'm getting to my ruling and how I'm getting to my ruling and being open and candid with both of you. But that's a built-in problem with class actions. They have achieved a beneficial result. The difficult[y] I am locked into is that I have got to follow the law of the case. I have got the Supreme Court that's telling me what to do. . . .

. . . .

MR. DeBRY: Your Honor –

THE COURT: You can take exceptions after I get done. I'm trying to –

MR. DeBRY: I might note that I do have an exception to take at this time before you give your verdict in this matter.

THE COURT: I haven't given a verdict.

Prudential did not object during the course of the exchange. Judge Rigtrup rendered his decision in favor of the Madsens and awarded them damages of $134.70.

After the ruling, Judge Rigtrup asked if either side wished to take any exceptions. Prudential's attorney stated only that an appeal was anticipated before any class issues were addressed. However, no specific objection to Judge Rigtrup's qualifications was voiced.

Thirty-nine days after Judge Rigtrup announced his decision, Prudential raised its first formal objection to the judge's qualifications to hear the case by filing a motion for disqualification under Rule 63(b) of the Utah Rules of Civil Procedure.[2] The motion was

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[2] Rule 63(b) reads:

(b) *Disqualification.* Whenever a party to any action or proceeding, civil or criminal, or his attorney shall make and file an affidavit that the judge before whom such action or proceeding is to be tried or heard has a bias or prejudice, either against such party or his attorney or in favor of any opposite party to the suit, such judge shall proceed no further therein, except to call in another judge to hear and determine the matter.

Every such affidavit shall state the facts and the reasons for the belief that such bias or prejudice exists, and shall be filed as soon as practicable after the case has been assigned or such bias or prejudice is known. If the judge against whom the affidavit is directed questions the sufficiency of the affidavit, he

(Continued on following page)

assigned to the then-presiding judge of the Third District, the Honorable Philip Fishler. Judge Fishler held several hearings on the motion and considered testimony, portions of the trial transcript, affidavits, and memoranda in reaching his decision. Judge Fishler ruled that Prudential's motion was timely, that the possibility existed that Judge Rigtrup may have a financial interest in the outcome of the case, and that Judge Rigtrup's impartiality might reasonably be questioned. Judge Fishler expressly found no actual bias on the part of Judge Rigtrup, but ordered him disqualified solely on the appearance of bias. After the case was assigned to another judge for retrial, we granted plaintiffs' request for an interlocutory appeal of Judge Fishler's order.

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shall enter an order directing that a copy thereof be forthwith certified to another judge (naming him) of the same court or of a court of like jurisdiction, which judge shall then pass upon the legal sufficiency of the affidavit. If the judge against whom the affidavit is directed does not question the legal sufficiency of the affidavit, or if the judge to whom the affidavit is certified finds that it is legally sufficient, another judge must be called in to try the case or determine the matter in question. No party shall be entitled in any case to file more than one affidavit; and no such affidavit shall be filed unless accompanied by a certificate of counsel of record that such affidavit and application are made in good faith.

I.

The Madsens contend that Prudential waived its objections to Judge Rigtrup's qualifications by failing to make a timely objection at the time of the judge's exchange with counsel, thereby giving Prudential the advantage of waiting to see if the ruling was favorable and, if not, of moving to disqualify. In addition, Prudential waited an extended period to file its motion to disqualify.

While a motion to disqualify a judge should not be undertaken lightly, it must be made promptly. A party who has a reasonable basis for moving to disqualify a judge may not delay in the hope of first obtaining a favorable ruling and then complain only if the result is unfavorable. Not only is such a tactic unfair, but it may evidence a belief that the judge is not in fact biased. Furthermore, delay imposes unnecessary disruption on both the judicial system and litigants. A disqualification proceeding is a collateral attack on the substantive action, it disrupts orderly litigation, and it necessarily results in significant additional costs to the parties. Accordingly, a party must move with dispatch once a basis for disqualification is discovered. *See Duplan Corp. v. Deering Milliken, Inc.*, 400 F.Supp. 497, 508-10 (D.S.C.1975); *Hunnicutt v. Hunnicutt*, 248 Ga. 516, 518, 283 S.E.2d 891, 893 (1981). *See generally* L. Abramson, *Judicial Disqualification Under Canon 3C of the Code of Judicial Conduct* 11-12 (1986) [hereinafter L. Abramson, *Judicial Disqualification*].

Timeliness is essential in filing a motion to disqualify.[3] In Utah, disqualification motions in civil proceedings are governed by Rule 63(b) of the Utah Rules of Civil Procedure (set out in footnote 2). That rule requires that a disqualification motion "shall be filed as soon as practicable after the case has been assigned or such bias or prejudice is known." The issue in this case is whether Prudential's failure to raise the issue during the colloquy with the judge before the ruling, its failure to object after the oral ruling was made when objections were invited by Judge Rigtrup, and Prudential's delay of thirty-nine days after the trial to file its disqualification motion meet the "as soon as practicable" requirement of Rule 63(b).

Federal cases require that motions to disqualify must be made as soon as the facts which form the basis for the disqualification become known. *See*

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[3] Some jurisdictions impose specific time limitations on some disqualification motions. *See, e.g.*, 28 U.S.C. § 144 (1982) (affidavit of bias must be filed not less than ten days before the beginning of the term at which the proceeding is to be heard); Alaska Stat. § 22.20.022(c) (1984) (affidavit for peremptory removal of judge must be filed within 5 days after the case is at issue or within 5 days after the issue is assigned to a judge); Me.Rev.Stat.Ann. title 14, § 1103 (1980 & Supp.1988) (petition for change of judge must be filed within ten days after service of complaint or other application for which equitable relief is sought); Minn.R.Civ.P. 63.03 (notice to remove judge must be filed within ten days after a party receives notice of which judge is presiding at the trial or hearing, but no later than commencement of the trial or hearing).

United States v. Studley, 783 F.2d 934, 939 (9th Cir.1986) ("a motion for recusal filed weeks after the conclusion of a trial is presumptively untimely absent a showing of good cause for its tardiness"); *Singer v. Wadman,* 745 F.2d 606, 608 (10th Cir.1984), *cert. denied,* 470 U.S. 1028, 105 S.Ct. 1396, 84 L.Ed.2d 785 (1985) (motion to disqualify filed one year after complaint and after adverse rulings of trial court was untimely); *Wood v. McEwen,* 644 F.2d 797, 802 (9th Cir.1981), *cert. denied,* 455 U.S. 942, 102 S.Ct. 1437 (1982) (delay of sixteen months after grounds for disqualification arose made motion to disqualify untimely); *United States v. Patrick,* 542 F.2d 381, 390 (7th Cir.1976), *cert. denied,* 430 U.S. 931, 97 S.Ct. 1551, 51 L.Ed.2d 775 (1977) ("The law is well settled that one must raise the disqualification of the judge at the earliest moment after knowledge of the facts demonstrating the basis for such disqualification."); *Satterfield v. Edenton-Chowan Bd. of Educ.,* 530 F.2d 567, 574 (4th Cir.1975) ("One must raise the disqualification of the trier, whether he be a judge, an administrator, or an arbitrator, at the earliest moment after knowledge of the facts."); *Davis v. Cities Serv. Oil Co.,* 420 F.2d 1278, 1282 (10th Cir.1970) (motion to disqualify filed a month after the case was decided against movants is too late); *Duplan Corp. v. Deering Milliken, Inc.,* 400 F.Supp. 497, 510 (D.S.C.1975) ("a recusal motion must be made at counsel's *first opportunity after discovery* of the disqualifying facts" (emphasis in original)).

State courts have also imposed stringent timeliness requirements. *See, e.g., Wakefield v. Stevens,* 249 Ga. 254, 255, 290 S.E.2d 58, 60 (1982) (motion to disqualify untimely if not "filed promptly and without delay, at the first opportunity after . . . [learning] of the grounds for disqualification" (quoting *State v. Fleming,* 245 Ga. 700, 705, 267 S.E.2d 207, 210 (1980) (Hill, J., concurring))); *Carpenter v. State,* 223 Kan. 523, 525, 575 P.2d 26, 29 (1978) (affidavit of prejudice should be filed as soon as a party "becomes aware of the facts giving rise to the challenge"). The rule is stated in 46 Am.Jur.2d *Judges* § 202, at 225-26 (1969):

> It is a well-recognized rule that an application for the disqualification of a trial judge must be filed at the earliest opportunity. The courts generally apply this rule with strictness against a party who, having knowledge of facts constituting a disqualification, does not seek to disqualify the judge until an unfavorable ruling has been made.

(Footnotes omitted).

While the Utah rule imposes no specific time limitation on the filing of a motion for disqualification, timeliness is still essential. To be timely, a motion to disqualify should be filed at counsel's first opportunity after learning of the disqualifying facts. Only if good cause for a delay is demonstrated in the motion seeking disqualification should a delinquent motion even be considered. *See Davis,* 420 F.2d at 1282; *Duplan Corp.,* 400 F.Supp. at 509-10.

Prudential's motion to disqualify Judge Rigtrup was not timely. Prudential claims that its first notice of bias on Judge Rigtrup's part occurred in his statement prior to announcing his ruling. However, Prudential's attorney did not object to the judge's continued participation in the case, as did opposing counsel, nor did Prudential ask for a continuance to consider disqualification. Prudential's attorney merely responded "that this is news to me" and then, after further dialogue with the judge, allowed the proceedings to continue without objection. By contrast, the *Madsens' counsel* did object to Judge Rigtrup's continuation as trial judge.

Prudential claims that Judge Rigtrup seemed determined to quell all interruptions as evidenced by his repeated admonition to plaintiffs' counsel to "sit down." Nevertheless, the record set out above demonstrates that plaintiffs' counsel was able to object. Beyond that, moments after Judge Rigtrup had delivered his oral ruling, he specifically afforded Prudential another opportunity to object: "Do you desire to make any further exceptions. . . ." Prudential's attorney responded: "Well, what I'm suggesting is that I expect that there will be an appeal before we get into the class issues, and I would anticipate findings and a judgment be presently entered in favor of Mr. Madsen." However, no mention was made of "recusal" or "disqualification."

Prudential asserts that it did object at trial, but our review of the record discloses no objection. On the

contrary, it discloses Prudential's apparent acquiescence in Judge Rigtrup's rendering a decision.

Finally, Prudential waited thirty-nine days after the ruling to file a formal motion to disqualify. Prudential argues that it had good cause for the delay. It contends that the lengthy delay was necessary to review personal notes, discuss the matter with other counsel in related cases, discuss the matter with Prudential's officers, and order, receive, and review a partial transcript. However, the review of the attorney's notes and the discussions with others should have consumed no more than a day or two. We doubt that the transcript was essential; in any event, all the facts relating to disqualification were known to Prudential's attorney at the close of the proceedings and an affidavit of prejudice and motion to disqualify could have been prepared with only a knowledge of those facts. We see no reason why the affidavit of prejudice and motion to disqualify should have taken more than ten days to prepare and file, especially since this case was at an advanced stage. Prudential failed to act with sufficient promptness in a matter which, by its very nature, requires promptness.

In sum, Prudential's motion to disqualify was not filed "as soon as practicable after . . . bias or prejudice is known," as required by Rule 63(b). Indeed, for all that appears, Prudential was not convinced at the time of the ruling that Judge Rigtrup should have recused himself.

II.

Given the importance of impartiality and the duty of a judge to recuse him- or herself *sua sponte* when necessary, we next address the issue of whether Judge Rigtrup should have disqualified himself on his own motion. In this context, we analyze the issues of apparent and actual bias raised by Prudential and addressed by Judge Fishler in his ruling.

Standards for judicial disqualification are established by statute and the Code of Judicial Conduct, which this Court adopted in 1974 and which is patterned after the ABA Code of Judicial Conduct of 1972. Utah Code Ann. § 78-7-1 (1987) provides for disqualification if the judge is a party, has an interest in a case, is related to either party, or has been an attorney for either party in the action.[4] The statute

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[4] Utah Code Ann. § 78-7-1 reads in full:

Disqualification for interest or relation to parties.

Except by consent of all parties, no justice, judge or justice of the peace shall sit or act as such in any action or proceeding:

(1) to which he is a party, or in which he is interested.

(2) when he is related to either party by consanguinity or affinity within the third degree, computed according to the rules of the common law.

(3) when he has been attorney or counsel for either party in the action or proceeding.

But the provisions of this section shall not apply to the arrangement of the calendar or the regulation of

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allows a waiver of disqualification if both parties consent, a point not at issue here.

Canon 3 C of the Code of Judicial Conduct (hereafter "Code") is more comprehensive than the statute in prescribing instances when judicial disqualification is warranted. In this case, the parties have based their arguments for and against disqualification on the Code. For this reason, we address the disqualification issues in the context of the Code.

The Madsens contend that the Code is an ethical code only and that a violation of the Code should not result in the invalidation of all of a judge's previous rulings. They argue that a violation should result only in discipline of the judge and not in a penalty to an innocent party who may have expended large amounts of time and money only to have a large part of the lawsuit invalidated because of a judicial disqualification. While most of the Code is aimed exclusively at the regulation of judicial behavior, Canon 3 C not only regulates judicial conduct, but it also seeks to avoid unfairness by insuring each litigant an impartial judge. Because we conclude that disqualification of the trial judge was not appropriate, we do not address further the issue of retroactive invalidation of a trial judge's rulings.

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the order of business, nor to the power of transferring the action or proceeding to some other court.

Prudential argues that Judge Fishler was correct in disqualifying Judge Rigtrup because Judge Rigtrup had personal knowledge of disputed evidentiary facts, displayed bias against Prudential, and had a financial interest in the outcome of the case. These allegations impute actual bias, but Judge Fishler specifically found no actual bias.[5] Moreover, as shown

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[5] Obviously, actual bias need not be found to support disqualification. *See State v. Neeley,* 748 P.2d 1091, 1094 (Utah 1988). An appearance of bias or prejudice is sufficient for disqualification, but even disqualification because of appearance must have some basis in fact and be grounded on more than mere conjecture and speculation. In close cases, disqualification is the favored course of action. However, disqualification is not automatic and the basis for disqualification should be thoroughly examined, especially in cases such as this which are at an advanced stage of the litigation process. *See, e.g., In re Virginia Elec. & Power Co.,* 539 F.2d 357, 364 (4th Cir.1976). As is demonstrated elsewhere in this opinion, close examination of Prudential's allegations against Judge Rigtrup show them to be without merit. Therefore, there was no basis in this case for disqualification.

We note that disqualification due to the appearance of bias or prejudice seems more amenable to prospective application. The purpose of disqualification based on appearance of bias is "to promote public confidence in the judicial system by avoiding even the appearance of partiality." *Health Services Acquisition Corp. v. Liljeberg,* 796 F.2d 796, 800 (5th Cir.1986), *aff'd,* 486 U.S. 847, 108 S.Ct. 2194, 100 L.Ed.2d 855 (1988). In *Liljeberg v. Health Services Acquisition Corp.,* 486 U.S. 847, 108 S.Ct. 2194, 2202-03, 100 L.Ed.2d 855 (1988), the United States Supreme Court concluded that disqualifying facts which a federal district judge should have known but which he had forgotten were sufficient to disqualify the judge under the federal statute. However, the federal statute in question, 28 U.S.C. § 455(a) (1982), requires disqualification for an appearance of bias.

(Continued on following page)

below, none of Prudential's allegations of bias withstands scrutiny.

A.

First, Prudential argues that Judge Rigtrup had personal knowledge of disputed evidentiary facts and, thus, violated Canon 3 C(1)(a). The issue before Judge Rigtrup was whether Prudential earned a net profit on the Madsens' budget payments. Prudential claimed a net loss in the handling of such funds. Prudential asserts that it had waived insurance premium payments of certain borrowers, including Judge Rigtrup, in 1977 and gave those borrowers the option of continuing their escrow accounts or discontinuing them altogether in 1979. For that reason, Prudential asserts, the judge had independent knowledge of the disputed issue from which Judge Rigtrup "jumped to the conclusion in his ruling that Prudential could have and would have discontinued the Madsens' reserve, or otherwise changed its handling procedures, rather than lose money in requiring them."

Judge Fishler was not persuaded that Judge Rigtrup had any knowledge concerning the facts in dispute in this case and found that this allegation would not support a claim of bias. Judge Fishler was

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Canon 3 C(1) makes disqualification based on an appearance of bias discretionary ("A judge *should* disqualify himself . . .") (emphasis added).

correct. Although Judge Rigtrup had knowledge of his own dealings with Prudential some six and eight years before the trial, that knowledge did not bear on the issue of whether Prudential made a profit on the budget payment accounts. Prudential cites no record support to the contrary.

B.

Next, Prudential argues that remarks made by Judge Rigtrup just before delivering his ruling evidenced prejudice. Prudential specifically asserts here, as it did before Judge Fishler, that the remarks made by the judge, including the comment, "I have cussed financial institutions, . . ." revealed a bias that warranted disqualification. Judge Fishler's memorandum decision does not mention this allegation as a basis for his disqualification order.

Concededly, Judge Rigtrup was somewhat less than diplomatic in expressing what his thinking had been many years ago about financial institutions and how his thinking had evolved over the years. Nevertheless, Judge Rigtrup's own remarks in context explain the isolated instances thought by Prudential to show bias. The judge stated:

> I think I've made general comments throughout that I have cussed financial institutions, and customers do simply because they see inherent injustice about that. And my perspective today, after 23 years [have] passed, has become much, much different at the end

of the 23 years. Far before that I could see the cost of money was markedly greater, and that I would be a damn fool to prepay. So I paid faithfully every month for 25 years, and not a day sooner or a day later. And I'm just commenting generally in terms of unjust or whatever. The tension is between that to be gained and that to be lost, I suppose, in my eyes. And I have a feeling that class actions are a form of champerty and maintenance in that the one that substantially gains is the lawyer or the expert. Mr. Madsen stands to gain little, except he has struck a blow for freedom, I suppose, in the form that the consumer has achieved balance.

Later the judge stated:

The tension is that in terms of the magnitude of the wear, what is to be gained by Mr. Madsen is de minimis. On the other hand, if the Court looks at economic realities, the high cost of money, high cost of labor and high cost of everything else, there is a societal interest in maintaining healthy, vital financial institutions that have the ability to fund building construction, homes, and so forth, in our community. And I simply observe that probably the savings and loan associations have been very instrumental and important in that particular process. I simply make those as an overview statement say to [sic] what has troubled me, and it's trouble[d] me for a long time.

Canon 3 C(1)(a) states that a judge should disqualify himself if he has "personal bias or prejudice concerning a party." Although litigants are entitled to a judge who will hear both sides and decide an issue on the merits of the law and the evidence presented, they are not entitled to a judge whose mind is a clean slate. Each judge brings to the bench the experiences of life, both personal and professional. A lifetime of experiences that have generated a number of general attitudes cannot be left in chambers when a judge takes the bench. Refusing to disqualify himself in *Laird v. Tatum,* 409 U.S. 824, 93 S.Ct. 7, 34 L.Ed.2d 50 (1972), Justice Rehnquist responded to a motion to recuse *nunc pro tunc:*

> Proof that a Justice's mind at the time he joined the Court was a complete *tabula rasa* in the area of constitutional adjudication would be evidence of lack of qualification, not lack of bias.
>
> . . . .
>
> [N]either the oath, the disqualification statute, nor the practice of the former Justices of this Court guarantees a litigant that each judge will start off from dead center in his willingness or ability to reconcile the opposing arguments of counsel with his understanding of the Constitution and the law.

Id. at 835, 838-39, 93 S.Ct. at 14, 15-16 (memorandum opinion of Rehnquist, J.) (emphasis in original). One commentator has stated:

> Supreme Court Justices are strong minded men, and on the general subject matters which come before them, they do have propensities; the course of decision cannot be accounted for in any other way.

J. Frank, *Disqualification of Judges: In Support of the Bayh Bill,*35 Law & Contemp. Probs. 43, 48 (1970). Obviously, the same is true for all judges. Concerning comments made in court during a case, a commentator stated:

> The traditional judicial view is that if a judge can be disqualified for bias following a comment or ruling during the court proceedings, there is no limit to disqualification motions and there would be a return to "judge shopping." Any judicial comment or ruling gives the appearance of partiality in the broadest sense to the adversely affected party. Suppose a judge who is the trier of fact comments during a hearing that a parent has had the opportunity to improve himself in order to make a home for his child but has made no effort to do so. Can the judge be disqualified for bias and prejudice? Whenever a judge hears any evidence, he develops an attitude which may change as the evidence develops. As long as the judge decides the case only after *all* the evidence is submitted, there appears to be no harm in such a comment. Such judicial comments made before a jury would constitute an improper expression of opinion on the evidence, but those statements made out of their hearing do not require recusal.

L. Abramson, *Judicial Disqualification,* at 23 (emphasis in original) (footnotes omitted). As long as a judge does not allow the "propensities" to obscure the evidence and will decide the case only after all the evidence is heard, then disqualification is generally not warranted by a judge's comments. *See Banks v. Department of Human Resources,* 141 Ga.App. 347, 348-49, 233 S.E.2d 449, 450 (1977), *overruled on other grounds, Chancey v. Department of Human Resources,* 156 Ga.App. 338, 340, 274 S.E.2d 728, 730 (1980).

Judge Rigtrup's remark that he had "cussed financial institutions" was simply a statement about an attitude he had had many years earlier, at a time when he was less knowledgeable about the operations of financial institutions. Viewed in its entirety and in the context in which that statement was made, there is no evidence of disqualifying bias in Judge Rigtrup's remarks. Indeed, it appears that Prudential saw no impropriety at the time the remarks were made, as demonstrated by its failure to object.

C.

Prudential next contends that because Judge Rigtrup was at one time a Prudential borrower, he had a financial interest in the outcome of the case. Prudential claims that the judge is either a "potential" member of the existing plaintiff class or a "potential" member of an alleged plaintiff class which has never been certified. This "potential" membership, Prudential claims, gives Judge Rigtrup sufficient

financial interest in the outcome of the case to warrant disqualification. Prudential asserts that amended complaints filed by the Madsens have added new legal theories to the case and have sought enlargement of the plaintiff class. The result, Prudential claims, is a plaintiff class whose boundaries are imprecise.

Notwithstanding Prudential's assertions, this case has a precisely defined plaintiff class, consisting of Prudential borrowers whose trust deeds contain language identical to the Madsens' trust deed. The class was certified by Judge Croft in 1977. Prudential does not argue, and we find nothing in the record to indicate, that Judge Rigtrup is a member of that class. While it is true that the Madsens did seek to enlarge the class, a new plaintiff class has never been certified. Allegations alone do not act to enlarge an existing class.

Judge Fishler held that Judge Rigtrup "*may* therefore *have a financial interest* which would be substantially affected by the outcome of the proceeding as defined under Canon 3C(1)(c)." (Emphasis added.) Judge Fishler erred. Judge Fishler and both sides on appeal have overlooked a critical point – the meaning of the term 'financial interest" in Canon 3 C(3)(c).

Canon 3 C(3)(c) states that "'*financial interest' means ownership* of a legal or equitable interest, however small, or a relationship as director, advisor, or other active participant in the affairs of a

party. . . ." (Emphasis added). In other words, without an ownership interest, no financial interest exists.

In *Virginia Elec. & Power Co. v. Sun Shipbldg. & Dry Dock Co.*, 407 F.Supp. 324 (E.D.Va.), *vacated sub nom. on other grounds In re Virginia Elec. & Power Co.*, 539 F.2d 357 (4th Cir.1976), a trial judge was asked to disqualify himself because he was a customer of the plaintiff public utility, and a verdict favorable to the plaintiff could result in a personal benefit to the judge of approximately $100 realized as a reduction in utility rates. The judge stated:

> Clearly, whatever interest the Court may have in the subject matter in controversy, it does not constitute a "financial interest" as defined [by the Code of Judicial Conduct and 28 U.S.C. § 455]. It has "ownership" of no interest – legal or equitable. . . . [T]he Court actually has "a vague and undefined interest, not ownership, in a credit or accounting adjustment. . . ."

407 F.Supp. at 327. The United States Court of Appeals for the Fourth Circuit reversed on other grounds but stated in its opinion that the trial judge correctly concluded that "he did not 'own' a legal or equitable interest in the subject matter." *In re Virginia Elec. & Power Co.*, 539 F.2d 357, 366 (4th Cir.1976). The appellate court noted that the trial judge's interest was analogous to a "bare expectancy" in property law and concluded that "Judge Warriner 'owned' just what the owner of a bare expectancy has – nothing at all." *Id.* at 367.

Judge Rigtrup also owned nothing. Therefore, he had no financial interest in the case as defined by Canon 3 C(3)(c), and disqualification on this basis was unwarranted.

D.

Finally, while Prudential has not raised the issue, we briefly examine whether Judge Rigtrup's disqualification would be warranted under the portion of Canon 3 C(1)(c) which calls for disqualification when the judge or a close relative has "any other interest that could be substantially affected by the outcome of the proceeding. . . ." The Reporter for the Code of Judicial Conduct interpreted "any other interest" to mean an economic interest. E. Thode, *Reporter's Notes to Code of Judicial Conduct* 63-67 (1973). Unlike the term "financial interest," "any other interest" does not require ownership and includes lesser economic interests. At least one trial judge has disqualified himself after finding that "any other interest" includes the possibility of receiving a $100 rebate on utility payments. *Virginia Elec. & Power Co.*, 407 F.Supp. 324. It could therefore be argued that Judge Rigtrup's potential membership in an alleged class constitutes "any other interest" and requires disqualification.

Although the term "any other interest" is usually confined to economic interests, further definition of

the exact types of economic interests which fall under the ambit of the term is difficult.[6]

In any event, the interest must be "substantially affected" to require disqualification. Professor Wright has stated: "The concept [of 'any other interest'] is necessarily an imprecise one. It has been suggested that it should be read 'to depend on the interaction of two variables: the remoteness of the interest and its extent or degree.'" C. Wright, A. Miller, & E. Cooper, 13A *Federal Practice and Procedure* § 3547, at 603 (1984) (footnotes omitted). Another frequently cited article has illustrated the point as follows:

> If the interest strongly resembles a direct interest – for example, stock held in a subsidiary (or parent) of the corporate party – any amount should disqualify, just as does any stock held in the party itself. As the interest becomes less direct, such as that in an enterprise carrying on business with the party, only if the extent of the interest is itself substantial can the judge's impartiality reasonably be questioned.

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[6] For a discussion of the few cases which classify noneconomic interests as "any other interest," see L. Abramson, *Judicial Disqualification*, at 65; C. Wright, A. Miller & E. Cooper, *13A Federal Practice and Procedure* § 3547, at 605 (1984). *See also Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796, 800 n. 1 (5th Cir.1986), *aff'd*, 486 U.S. 847, 108 S.Ct. 2194, 100 L.Ed.2d 855 (1988); *Liljeberg v. Health Services Acquisition Corp.*, 486 U.S. 847, 108 S.Ct. 2194, 2206, 100 L.Ed.2d 855 (1988).

Note, *Disqualification of Judges and Justices in the Federal Courts,* 86 Harv.L.Rev. 736, 753 (1973) (footnote omitted).

Courts which have considered the issue have followed this approach, examining both the nature of the interest and the extent of the interest. In *In re Virginia Elec. and Power Co.,* the Fourth Circuit relied on that approach to hold that a trial judge's interest in a possible rebate on utility payments was a de minimis interest and that disqualification was not required. 539 F.2d at 368. *See also Alaska Oil Co. v. Alaska,* 45 Bankr. 358, 361-62 (D.Alaska 1985).

Aetna Life Ins. Co. v. Lavoie, 475 U.S. 813, 106 S.Ct. 1580, 89 L.Ed.2d 823 (1986), is similar in significant respects to this case. In *Aetna,* the insurer discovered after an opinion had been issued that a justice of the Alabama Supreme Court who was the author of the per curiam opinion had filed two actions against insurers in state court alleging issues nearly identical to those presented to the court on appeal. One of the suits involved only that justice. The other was a class action in which the class apparently included all members of the Alabama Supreme Court. The United States Supreme Court addressed separately the disqualification issue with respect to the individual justice and the other members of the Alabama court as members of the uncertified class. The Court held that the individual justice should have recused himself because the opinion which he had authored had "the clear and immediate effect of enhancing both the legal status and the settlement

value of his own case." 475 U.S. at 824, 106 S.Ct. at 1586. However, the Court refused to hold that the other members of the Alabama court should have been disqualified because of their potential status as members of a class of plaintiffs in a class action lawsuit. The United States Supreme Court stated:

> Any interest that they might have had when they passed on the rehearing motion was clearly highly speculative and contingent. At the time, the trial court had not even certified a class, let alone awarded any class relief of a pecuniary nature. . . . At some point, "[t]he biasing influence . . . [will be] too remote and insubstantial. . . ."

475 U.S. at 826, 106 S.Ct. at 1558 (quoting *Marshall v. Jerrico, Inc.*, 446 U.S. 238, 243, 100 S.Ct. 1610, 1613, 64 L.Ed.2d 182 (1980)).

In this case, Judge Rigtrup is, at most, a potential member of an alleged class. As such, his position is similar to eight of the nine justices of the Alabama Supreme Court in *Aetna* who might have found themselves class members. Under those circumstances, the United States Supreme Court refused to find in favor of disqualification, and we do likewise here. If any existing certified classes are expanded to include Judge Rigtrup or any new class were certified that included him, Judge Rigtrup would have to disqualify himself from further proceedings. We assume, of course, that he would not undertake to rule on a motion to certify a class or to expand a class

if he could thereby become a party by virtue of his ruling.

REVERSED AND REMANDED.

HOWE, Associate C.J., and DURHAM, J., concur.

ZIMMERMAN, J., concurs in the result.

HALL, C.J., does not participate herein.

APPENDIX E

635 F.2d 797

United States Court of Appeals,
Tenth Circuit.

Richard MADSEN and Nancy Madsen, his wife, for themselves and all others similarly situated,
Plaintiffs-Appellants,

v.

PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION, for itself and all others similarly situated, Defendant-Appellee,
Utah Bankers Association, Intervenor-Appellee.

Richard MADSEN and Nancy Madsen, for themselves and all others similarly situated,
Petitioners,

v.

Honorable Aldon J. ANDERSON, Judge of the United States District Court for the District of Utah, Central Division, Respondent.

Nos. 79-1362, 79-1535.

Argued May 6, 1980.
Decided Dec. 3, 1980.
Rehearing Denied Jan. 23, 1981.

Robert J. DeBry, Salt Lake City, Utah, for plaintiffs-appellants.

Joseph J. Palmer, Salt Lake City, Utah (Reid E. Lewis, Salt Lake City, Utah, with him on the brief) of Moyle & Draper, Salt Lake City, Utah, for defendant-appellee.

Peter W. Billings, of Fabian & Clendenin, Salt Lake City, Utah, for intervenor-appellee.

Milan C. Miskovsky, Gen. Counsel, Harvey Simon, Acting Associate Gen. Counsel, Michael L. Seablot, Trial Atty., of Federal Home Loan Bank Board, Washington, D. C., on the brief for amicus curiae Federal Home Loan Bank Board.

Before LOGAN, PECK* and SEYMOUR, Circuit Judges.

SEYMOUR, Circuit Judge.

The Madsens, plaintiffs-appellants, borrowed money from Prudential Federal Savings & Loan Association (Prudential) to purchase a home in 1964. Pursuant to this loan, the Madsens signed a trust deed[1] requiring them to make "budget payments" of

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* Of the United States Court of Appeals for the Sixth Circuit sitting by designation.

[1] The trust deed provides in pertinent part:

"In addition to the monthly payments as provided in said note, the TRUSTOR agrees to pay to the BENEFICIARY, upon the same day each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to be adjusted from time to time as required, and said budget payments are hereby pledged to the BENEFICIARY as additional security for the full performance of this deed of trust and the note secured hereby. The budget payments so accumulated may be withdrawn by the BENEFICIARY for the payment of taxes or insurance premiums due on the premises. The BENEFICIARY may at any time, without notice, apply said budget payments to the payment of sums due under the terms of this deed of trust and the note secured hereby or either of them.

(Continued on following page)

one-twelfth of the annual estimated taxes and insurance along with their monthly payments of principal and interest. Under the agreement, these budget payments were pledged as additional security for repayment of the loan. The funds were accumulated in a reserve account and used annually for the payment of taxes and insurance.

On March 3, 1975, the Madsens[2] filed a class action[3] in Utah state court seeking to recover interest realized from Prudential's use of the escrowed funds, based on claims of breach of contract and unjust enrichment. The state trial court granted Prudential's motion for summary judgment. In January 1977, the Utah Supreme Court reversed the summary judgment and remanded for further proceedings. It held that the trust deed contained the essential elements of a pledge, and that under Utah common law a pledgee must account to the pledgor for profits resulting from the use of the pledged property. In October 1977, the Madsens amended their complaint to ask for an accounting and recovery of the profits earned by Prudential on the escrowed amounts. This

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TRUSTOR'S failure to pay said budget payments shall constitute a default under this trust."

App., vol. I, at 5.

[2] The original complaint named Richard Madsen only as plaintiff. An amended complaint was filed April 10, 1975, joining his wife Nancy.

[3] Numerous issues regarding the classes named in these proceedings have been raised on appeal. They are not relevant to our disposition of this case and are not addressed in our opinion.

amended complaint added a defendant class of lenders with similar escrow arrangements.

Meanwhile in April 1977, Prudential filed a separate action for declaratory relief in federal court, asserting that under 12 C.F.R. s 545.6-11(c)[4] (hereinafter referred to as section 545.6-11(c)), it is not required to pay interest or account to the Madsens on the escrowed funds. The complaint based jurisdiction on 28 U.S.C. s 1337[5] and sought a declaration of the

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[4] 12 C.F.R. s 545.6-11(c) provides:

"A Federal association which makes a loan on or after June 16, 1975, on the security of a single-family dwelling occupied or to be occupied by the borrower (except such a loan for which a bona fide commitment was made before that date) shall pay interest on any escrow account maintained in connection with such a loan (1) if there is in effect a specific statutory provision or provisions of the State in which such dwelling is located by or under which the State-chartered savings and loan associations, mutual savings banks and similar institutions are generally required to pay interest on such escrow accounts, and (2) at not less than the rate required to be paid by such State-chartered institutions but not to exceed the rate being paid by the Federal association on its regular accounts (as defined by Section 526.1 of this chapter). Except as provided by contract, a Federal association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph."(Emphasis added).

[5] 28 U.S.C. s 1337 provides:

"The district courts shall have original jurisdiction of any civil action or proceeding arising under any Act of Congress regulating commerce or protecting trade and commerce against restraints and monopolies."

rights and obligations of the parties to the trust deed. When the Madsens amended their state complaint, Prudential promptly filed a removal petition, alleging that the relief requested arises under and is controlled by federal law. The Utah Bankers Association, a trade association of commercial banks domiciled in Utah, intervened in the action, and the Federal Home Loan Bank Board filed an amicus curiae brief. The federal court denied the Madsens' motion to remand the case, consolidated the removed action and the declaratory judgment suit, and granted summary judgment in favor of Prudential.

On appeal, the Madsens contend, inter alia, that the federal court lacks jurisdiction over either the removed case or the declaratory judgment action. We agree, and reverse with directions to remand the removed action to state court and to dismiss the declaratory action.

I.

Removal Jurisdiction

Prudential sought removal pursuant to 28 U.S.C. s 1441(b), which provides in pertinent part:

> "Any civil action of which the district courts have original jurisdiction founded on a claim or right arising under the Constitution, treaties or laws of the United States shall be removable without regard to the citizenship or residence of the parties."

Jurisdiction was claimed under 28 U.S.C. s 1331[6] and section 1337 because the cause of action allegedly arose under the laws of the United States and Acts of Congress regulating commerce.

The Madsens contend their claim in state court is founded upon contract rights and obligations created by state law. They assert that Prudential retains the Madsens' budget payments for up to a year before using the funds to pay the taxes and insurance, that Prudential invests the funds in the interim and receives a profit, and that the Madsens are entitled to be paid the profits earned on the pledged funds. The Madsens point out that no federal law or regulation was invoked, relied on, attacked, or cited in their complaint. Consequently, they say, their claim did not arise under federal law.

Prudential and Intervenor argue, on the other hand, that the trust agreement between Prudential and the Madsens contains no express language requiring the payment of interest on the escrowed funds, and that the federal regulation does not

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[6] 28 U.S.C. s 1331(a) provides in pertinent part:

"The district courts shall have original jurisdiction of all civil actions wherein the matter in controversy exceeds the sum or value of $10,000, exclusive of interest and costs, and arises under the Constitution, laws or treaties of the United States."

We note that the same standards apply to whether the issue "arises under" federal law in both this section and section 1337.

contemplate interest payments under such circumstances. They say that interpretation of the agreement arises under federal law because Prudential is a regulated federal savings and loan association and Congress has preempted the area.

The conditions under which a suit may be said to "arise under" the laws of the United States were definitively set out in *Gully v. First National Bank,* 299 U.S. 109, 57 S.Ct. 96, 81 L.Ed. 70 (1936). There the Court stated that the required federal right or immunity must be an essential element of the plaintiff's cause of action, and that the federal controversy must be "disclosed upon the face of the complaint, unaided by the answer or by the petition for removal." *Id.* at 113, 57 S.Ct. at 98. It is beyond argument that a defense predicated upon federal law is not enough by itself to confer federal jurisdiction, even though the defense is certain to arise. *Pan American Petroleum Corp. v. Superior Court,* 366 U.S. 656, 663, 81 S.Ct. 1303, 1307, 6 L.Ed.2d 584 (1961); *Seneca Nursing Home v. Kansas State Board of Social Welfare,* 490 F.2d 1324, 1328 (10th Cir. 1974), *cert. denied*, 419 U.S. 841, 95 S.Ct. 72, 42 L.Ed.2d 69 (1974); *Warner Bros. Records, Inc. v. R. A. Ridges Distributing Co.,* 475 F.2d 262 (10th Cir. 1973).

In *Mountain Fuel Supply Co. v. Johnson,* 586 F.2d 1375, 1381 (10th Cir. 1978), *cert. denied*, 441 U.S. 952, 99 S.Ct. 2182, 60 L.Ed.2d 1058 (1979), we described the test for determining whether a complaint asserts, on its face, a substantial federal question:

> "A case 'arises' under the laws of the United States if it clearly and substantially involves a dispute or controversy respecting the validity, construction or effect of such laws which is determinative of the resulting judgment. *Shulthis v. McDougal,* 225 U.S. 561, 32 S.Ct. 704, 56 L.Ed. 1205 (1912). Thus, if the action is not expressly authorized by federal law, does not require the construction of a federal statute and/or regulation and is not required by some distinctive policy of a federal statute to be determined by application of federal legal principles, it does not arise under the laws of the United States for federal question jurisdiction. *Lindy v. Lynn,* 501 F.2d 1367 (3rd Cir. 1974)."

No argument has been made on appeal that the Madsens' claim is expressly authorized by federal law. Consequently, federal removal jurisdiction is established in this case only if the Madsens' claim requires the construction of a federal regulation or the application of federal law.

The federal trial court based its finding of jurisdiction on *North Davis Bank v. First National Bank,* 457 F.2d 820 (10th Cir. 1972). We find that case distinguishable. There the central issue in the complaint was whether the defendant's facility constituted a branch of a national bank. We noted that the Supreme Court in *First National Bank v. Dickinson,* 396 U.S. 122, 133, 90 S.Ct. 337, 343, 24 L.Ed.2d 312 (1969), held this determination to be a "threshold question of federal law." 457 F.2d at 822. Therefore

we held: "(t)his is not a case in which a federal statute is indirectly or collaterally involved but it is one having its source in and arising under (the McFadden Act) 12 U.S.C. s 36(f)." *Id.* at 823.

Here the basic issue in the Madsens' complaint is whether the contract between the Madsens and Prudential requires the payment of profits or interest on escrowed funds. Although construction of the federal regulation cited by Prudential may be relevant to the defense Prudential asserts, i. e., that section 545.6-11(c) does not require payment of interest, the meaning of the regulation is absolutely irrelevant to the Madsens' theory of recovery. Because the Madsens have predicated their suit upon rights created under state law, the fact that federal regulations may create a defense to recovery on such a claim is immaterial to a finding of federal question jurisdiction. *See Phillips Petroleum Co. v. Texaco,* 415 U.S. 125, 94 S.Ct. 1002, 39 L.Ed.2d 209 (1974); *Pan American Petroleum,* 366 U.S. at 662-64, 81 S.Ct. at 1307-13[illegible].

Prudential and Intervenor contend that removal jurisdiction exists because federal law has preempted state law in the area of federal savings and loan regulation. The amicus curiae brief supports the argument that the field of regulatory control over federal associations has been preempted. However, even if federal preemption were established, it would not confer jurisdiction when it is raised by the defendant to defeat a common-law contract claim brought in state court. *See Pan American Petroleum,* 366 U.S.

at 662-65, 81 S.Ct. at 1307-1309; *Washington v. American League of Professional Baseball Clubs,* 460 F.2d 654, 660 (9th Cir. 1972), and cases cited therein. In *Home Federal Savings & Loan Association v. Insurance Department,* 571 F.2d 423 (8th Cir. 1978), the court dismissed the case for lack of subject matter jurisdiction despite a federal preemption argument:

> "(T)he Commissioner's proceeding against Home Federal was based solely upon alleged violations of Iowa's insurance law and raised no federal question. Home Federal's allegations of preemption and failure to engage in the 'business of insurance,' asserted in its federal petition, actually are in the nature of defenses to the Commissioner's charges. Hence they will not suffice for federal question jurisdiction here. The case is basically simply an alleged violation of state law. It is not a federal case and is not converted to one by Home Federal's defenses to the state's basic allegations."

Id. at 427. Prudential's claim of federal preemption is in the nature of a defense to the Madsens' cause of action and cannot be the basis of federal question jurisdiction on removal.

It is also argued that the Madsens' claim arises under the laws of the United States because the contract must be interpreted under federal common law rather than state law. This is so, Prudential urges, because the regulation addressing the payment of interest by federal savings and loan associations,

section 545.6-11(c), states that "(e)xcept as provided by contract, a Federal Association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph." (Emphasis added). Prudential contends that the circumstances constituting a "contract" within the meaning of the federal regulation is a federal question.

It is true that the application of federal common law to a plaintiff's cause of action is sufficient to invoke federal jurisdiction and thus support removal. *See Illinois v. Milwaukee,* 406 U.S. 91, 100, 92 S.Ct. 1385, 1391, 31 L.Ed.2d 712 (1972). However, federal common law is not automatically applied to resolve all disputes in a field subject to pervasive federal regulation. "In deciding whether rules of federal common law should be fashioned, normally the guiding principle is that a significant conflict between some federal policy or interest and the use of state law in the premises must first be specifically shown." *Wallis v. Pan American Petroleum Corp.*, 384 U.S. 63, 68, 86 S.Ct. 1301, 1304, 16 L.Ed.2d 369 (1966). Here, it is vigorously argued that application of state law would create a significant conflict because federal policy requires uniform nationwide standards for the handling of escrow accounts by federal savings and loan associations. This argument founders on the very language of the regulation cited to support it. Section 545.6-11(c) provides that a federal savings and loan association shall pay interest on escrow accounts if a state statute requires such payments to be made by state-chartered institutions, or if

payments are required by contract. The regulation expressly anticipates that the obligation of a federal institution to pay interest on escrow accounts not only will vary from state to state, but from contract to contract. *See Johnson v. First Federal Savings & Loan Association,* 418 F.Supp. 1106, 1109 (E.D.Mich.1976). Any argument that federal policy requires nationwide uniformity with regard to this issue is untenable.[7] *See United States v. Yazell,* 382 U.S. 341, 86 S.Ct. 500, 15 L.Ed.2d 404 (1966).

Contractual obligations are created by state law. *See Gully,* 299 U.S. at 114-15, 57 S.Ct. at 98-99. *See also Pan American Petroleum v. Superior Court,* 366 U.S. at 662-663, 81 S.Ct. at 1307-1308. "The interpretation and enforcement of contracts is (sic) traditionally within the province of state courts," *Mariniello v. Shell Oil Co.,* 511 F.2d 853, 858 (3d Cir. 1975), and the general presumption is in favor of applying state law. Note: Federal Common Law, 82 Harv.L.Rev. 1512 (1969). Given the absence of a significant conflict between the federal policy expressed in section

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[7] We note Intervenor's argument that this case arises under federal law because the mortgage form must be approved by the regulatory agency, see 24 C.F.R. s 203.17, and because the mortgage must provide for monthly escrow payments for taxes and insurance, see 24 C.F.R. s 203.23(a). However, these regulations are silent on the issue of interest payments on escrow accounts, and therefore do not conflict with section 545.6-11(c), which allows interest to be required or prohibited by the individual contract terms. Accordingly, we reject the argument that the use of these forms mandates a uniform interpretation under federal law.

545.6-11(c) and the use of state law, we hold that state law is applicable in determining whether Prudential contracted to pay interest on the Madsens' escrow account.

Since no federal controversy was disclosed on the face of the Madsens' state court complaint, as amended, removal was improper and the consolidated case must be remanded to state court.

II.

Declaratory Judgment Jurisdiction

The question remains whether the federal court has subject matter jurisdiction over Prudential's declaratory judgment action. The federal complaint alleges that Prudential is a federal savings and loan association regulated by the Federal Home Loan Bank Board, that it makes residential real estate loans insured and guaranteed by federal agencies, and that it is not permitted to pay interest or to otherwise account for profits realized on escrowed funds paid by mortgagors "except as provided by applicable federal regulations." App., vol. II, at 180. It points out that the Madsens have filed a class action in state court seeking interest on the escrowed funds under the contractual arrangements between Prudential and its borrowers, that "(a) proper resolution of said controversy requires a declaration of the respective rights and obligations of the parties to said contractual arrangements," *id.* at 181, and that this

determination presents a question under federal laws regulating commerce or under federal common law.[8]

As we have noted, the federal regulation that Prudential cites in its complaint provides that interest shall be paid on escrow accounts if a statute in the state where the mortgaged property is located requires similar lending institutions to pay such interest. 12 C.F.R. 545.6-11(c), *supra* n. 4. The regulation also provides that a federal association has no other obligation to pay such interest "(e)xcept as provided by contract." *Id.* Consequently, the controversy underlying the federal declaratory judgment action is the same as in state court: whether Prudential is obligated by its contract with the Madsens to pay interest on the escrowed funds.

This court has consistently adopted the rationale set out by the Supreme Court in Public Service Commission of *Utah v. Wycoff Co.*, 344 U.S. 237, 248, 73 S.Ct. 236, 242-243, 97 L.Ed. 291 (1952):

> "Where the complaint in an action for declaratory judgment seeks in essence to assert a defense to an impending or threatened state court action, it is the character of the threatened action, and not of the defense, which will determine whether there is federal-question jurisdiction in the District

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[8] We have already concluded in part I, *supra*, that federal common law is not applicable to interpret the contract between Prudential and the Madsens.

> Court. If the cause of action, which the declaratory defendant threatens to assert, does not itself involve a claim under federal law, it is doubtful if a federal court may entertain an action for a declaratory judgment establishing a defense to that claim. This is dubious even though the declaratory complaint sets forth a claim of federal right, if that right is in reality in the nature of a defense to a threatened cause of action. Federal courts will not seize litigations from state courts merely because one, normally a defendant, goes to federal court to begin his federal-law defense before the state court begins the case under state law. (citations omitted)."

(Emphasis added). In *Monks v. Hetherington,* 573 F.2d 1164, 1167 (10th Cir. 1978), we applied the traditional view "that a party cannot by artful pleading anticipate a defense based on federal law and thus bring within federal jurisdiction an action that could not otherwise be heard in federal court." And in *Chandler v. O'Bryan,* 445 F.2d 1045, 1055-56 (10th Cir. 1971), we noted that this principle is particularly applicable where, as here, the state court action has been instituted and issues have been decided.

We held in part I, *supra*, that the federal preemption argument is defensive in nature. This is true whether the claim is made as the basis of removal or to support federal jurisdiction in a declaratory judgment action. *See, e. g., Home Federal Savings & Loan Association v. Insurance Department,* 571 F.2d 423

(8th Cir. 1978). This case is not like *Conference of Federal Savings & Loan Associations v. Stein,* 604 F.2d 1256 (9th Cir. 1979), *aff'd mem.*, 445 U.S. 921, 100 S.Ct. 1304, 63 L.Ed.2d 754 (1980), *First Federal Savings & Loan Association v. Greenwald,* 591 F.2d 417 (1st Cir. 1979), or others cited by Prudential, Intervenor, and amicus curiae, where state regulations directly conflict with federal regulations governing federal associations. No such conflict exists here.

The defensive nature of Prudential's claim is expressed throughout its complaint. It alleges that a state action has been brought seeking interest pursuant to the contractual arrangements between the parties, and that any order of the state court requiring Prudential to pay interest or otherwise account to the Madsens would be contrary to the federal regulations. If the Madsens had attempted to bring their action in federal court by anticipating or responding to Prudential's possible federal defense, the case would lack federal jurisdiction. *See Phillips Petroleum,* 415 U.S. at 128, 94 S.Ct. at 1004; *Skelly Oil Co.,* 339 U.S. 667, at 672, 70 S.Ct. 876, 879, 94 L.Ed. 1194; *Home Federal Savings & Loan Association,* 571 F.2d at 426-27. It is irrelevant for purposes of jurisdiction that "federal consent is the source of state authority." *Gully,* 299 U.S. at 116, 57 S.Ct. at 99; *Oklahoma ex rel. Wilson v. Blankenship,* 447 F.2d 687, 691 (10th Cir.), *cert. denied*, 405 U.S. 918, 92 S.Ct. 942, 30 L.Ed.2d 787 (1971).

Here as in *Gully* "(t)he most one can say is that a question of federal law is lurking in the background."

299 U.S. at 117, 57 S.Ct. at 99-100. Accordingly, we hold the court has no jurisdiction over the declaratory judgment complaint and the action must be dismissed.

Reversed.

APPENDIX F

558 P.2d 1337

Supreme Court of Utah.
Richard MADSEN and Nancy A. Madsen, his wife,
Plaintiffs and Appellants,
v.
PRUDENTIAL FEDERAL SAVINGS & LOAN ASSOCIATION, Defendant and Respondent.

No. 14530.

Jan. 14, 1977.

Robert J. DeBry, Salt Lake City, for plaintiffs-appellants.

Joseph J. Palmer, Salt Lake City, for defendant-respondent.

MAUGHAN, Justice:

On appeal is a summary judgment granted to defendant, hereafter Prudential, against plaintiffs, hereafter Madsen or trustors. The action is founded upon terms of a deed of trust; and was brought to determine the status of the parties, and the legal consequences pursuant to such terms. We reverse the summary judgment, and remand for further proceedings. Costs are awarded to Madsen. Statutory references are to U.C.A.1953.

Madsens are trustors, and defendant is both the trustee and beneficiary under a deed of trust executed September 21, 1964, for the purpose of securing a

promissory note in the sum of $16,800. The security conveyed was the home in which plaintiffs reside.

To protect the security, the trustors further agreed:

> 2. To keep the buildings and improvements on the above described premises insured against loss by fire, and such other casualties and in such forms of insurance, and in such amounts, and in such companies as may be required by and as may be satisfactory to the beneficiary, for the benefit of the beneficiary, and to pay the premiums therefor promptly when due, and the policies of insurance shall be held by the beneficiary, it being understood, however, that the beneficiary shall in no event be responsible for the sufficiency or form or substance of any policy of insurance, or for the solvency or sufficiency of any insurance company in respect to the insurance herein provided.
>
> * * *
>
> 4. To pay before delinquent all taxes and assessments affecting said property (including assessments on appurtenant water stock and costs, interest and penalties thereon); and all encumbrances, charges and liens, with interest and penalties on said property or any part thereof, which appear to be or are prior or superior hereto.
>
> In addition to the monthly payments as provided in said note, the trustor agrees to pay to the beneficiary, upon the same day

> each month, budget payments estimated to equal one-twelfth of the annual taxes and insurance premiums; said budget payments to be adjusted from time to time as required, and said *budget payments are hereby pledged to the beneficiary as additional security for the full performance of this deed of trust and the note secured hereby*. The budget payments so accumulated may be withdrawn by the beneficiary for the payment of taxes or insurance premiums due on the premises. The beneficiary may at any time, without notice, apply said budget payments to the payment of any sums due under the terms of the deed of trust and the note secured hereby or either of them. Trustor's failure to pay said budget payments shall constitute a default under this trust. (Emphasis supplied.)

Madsen's appeal is predicated on the theory that the monthly budget payments under provision 4 of the instrument constitute a common law pledge. They alleged defendant had invested this pledged property, and earned a substantial profit. An accounting is sought on the ground the substantial profits from the investment of the pledged funds constitute an unjust enrichment, entitling them to restitution.

The trial court ruled the funds accumulated, from the monthly budget payments, were not pledged property. Therefore, the law of pledge was not applicable.

In *Campbell v. Peter*[1] this court stated:

> A pledge is really one of the simplest forms of security. It is the passing of possession of a chattel by the owner thereof to the pledgee who is thereby entitled to hold it until the debt is paid or the obligation performed. (Citations)

We further cited with approval the definition in the Restatement Security, Sec. 1, p. 5, which provides:

> A pledge is a security interest in a chattel or an intangible represented by an indispensable instrument, the interest being created by a bailment for the purpose of securing the payment of a debt or the performance of some other duty.

Comment d. of Sec. 1, p. 10 states:

> The term "chattel" means any physical object which is capable of manual delivery and which is not the subject-matter of real property. It includes instruments and documents.

A deposit of money as security for the performance of a contract has been recognized as a valid pledge.[2]

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[1] 108 Utah 565, 568, 162 P.2d 754, 755 (1945).

[2] *Anderson v. Pacific Bank*, 112 Cal. 598, 44 P. 1063 (1896); *United States v. Harris*, USDC WD La.1966, 249 F.Supp. 221, 224; 68 Am.Jur.2d, Secured Transactions, Sec. 58, pp. 886-887.

> . . . it (is) of no consequence that the amount of funds subjected to the lien, and thus, the amount of the lien, may vary during the existence of the pledge. The amount is ascertainable at any given time, and thus the lien is perfected as to amount.[3]

In the current matter, plaintiffs, as the trustors, agreed to protect the security of Prudential by paying the insurance and taxes. Madsen agreed to pay the budget payments, and to pledge them to the beneficiary 'as additional security for the full performance' of the deed of trust and the note secured thereby.

The essential elements of a pledge are contained in the agreement, viz., the existence of a debt or obligation, a transfer of property to the pledgee, to be held as security and, if necessary, to be used to assure performance of the obligation. Furthermore, the payments accumulated, may, in the discretion of the beneficiary, be withdrawn for the payment of taxes, insurance premiums due, or any sum due under the deed of trust, or note. There is no contract right granted to Madsen to compel defendant to pay the insurance premiums or taxes. The payments accumulated may be retained as security or applied for the purposes stated. The primary obligation to pay the insurance, taxes, and any sum due under the deed of trust or note is Madsen's. The provisions of section 4

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[3] *United States v. Harris*, note 2 *supra*.

grant a security interest to Prudential, for the purpose of securing performance of trustors' obligations.

Madsen cites *Hoyt v. Upper Marion Ditch Company*[4] to establish the legal consequences, under a common law pledge, wherein profits accrue to pledgee; as a result of the possession of a pledged chattel. We there said it is the duty of a pledgee to collect the accruals, from the security, and apply them to the debt. We there explained: when the property pledged is of such a character as not to be lessened by use, the pledgee does not incur liability by using it; but, if from the use of it profits are derived, pledgee must, in the absence of a special agreement, account for them to the pledgor. There cited as authority was 21 R.C.L. 665-666, Sec. 28; the relevant provisions of which are:

> . . . If from the use of the property pledged profits are derived, the pledgee must in the absence of a special agreement to the contrary account therefor to the pledgor, and apply the net proceeds of such use to the extinction of the debt. So if any profits accrue from property held as collateral, such profits, while they may be collected and retained by the pledgee, must be credited to the pledgor, or applied to the sum due from him, as where dividends accrue on pledged stock, or

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[4] 94 Utah 134, 143, 76 P.2d 234 (1938).

> interest is collected on a security held as collateral.[5]

The foregoing principles of the law of pledge are not new. Indeed, Madsen's counsel cites the Code of Manu and that of Hammurabi, for early examples.[6] These principles have not been discarded. In our Uniform Commercial Code we find:

> Unless otherwise agreed, when collateral is in the secured party's possession
>
> * * *
>
> (c) the secured party may hold as additional security any increase or profits (except money) received from the collateral, but money so received, unless remitted to the debtor, shall be applied in reduction of the secured obligation; . . . .[7]

An excursus to 9-207, of the Uniform Commercial Code, illuminates the provision:[8]

> 2. Subsection (2) states rules, which follow common law precedents, and which apply, unless there is agreement otherwise, in typical situations during the period while the secured party is in possession of the collateral.

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[5] *See* 69 Am.Jur.2d Secured Transactions, s 223, pp. 58-59.

[6] I. A. Rocureck and J. S. Wigmore, Source of Ancient and Primitive Law, p. 401 (1915).

[7] 70A-9-207(2), U.C.A., 1953.

[8] 3 ULA, Uniform Commercial Code (Master Edition) s 9-207p. 123.

This principle is also set forth in the Restatement, Security, Sec. 27, p. 91:

> The pledgee has the duty to account to the pledgor for the increase or profits accruing to the pledgee as a result of the possession of the pledged chattel.

ELLETT and WILKINS, JJ., concur.

CROCKETT, Justice (dissenting).

I have no disagreement with the general proposition advocated by the plaintiffs, and as set forth in the main opinion, that where there is a simple pledge of property, which can be put to profitable use without lessening its value, and the pledgee uses it for a profit, the profit should inure to the benefit of the pledgor, unless the understanding of the parties is to the contrary. It is not my understanding that the position of the defendant or of the trial court is in disagreement therewith. That position briefly stated is this: That it is shown that both the plaintiffs and the defendant were fully aware of the manner in which this co-called monthly 'budget payment' of one twelfth of the taxes and insurance for the year was to be made and handled to insure payments of those essentials; that even though plaintiffs were so aware and considered this to be unfair, they did not then so state, nor make any request that interest should be paid thereon, but voluntarily entered into the contract fully and clearly setting forth the rights and obligations of the parties, but without the contract

containing any such covenant as to the payment of interest.

There are some elementary principles of contract law that should be given consideration here: that when parties negotiate on a subject matter and reduce their agreement to writing, it should be presumed to consolidate their entire understanding as to mutual rights and obligations on that subject matter;[1] and further, that the contract should be enforced and enforceable against each party only in accordance with the covenants expressed therein.[2]

Pertinent to the plaintiffs' demand for payment of interest on the 'budget payment' it is to be noted that the documentary evidence shows that over the years of their contract that account had an average balance of $275.42, which at an interest rate of 5% would produce $13.70 per year; and that the estimated cost to the bank of the collecting, accounting and disbursing of such 'budget payments' would be $16 per account per year.

When all of the foregoing is considered in the light of the principles of law set forth above, I think the trial court was justified in adopting the position essayed by the defendant: that if the plaintiffs had desired a covenant to pay interest on the 'budget

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[1] *Mawhinney v. Jensen*, 120 Utah 142, 232 P.2d 769.

[2] *See Jones v. Acme Bldg. Products*, 22 Utah 2d 202, 450 P.2d 743.

payment' they should have so stated and negotiated for such a covenant in the contract. But having failed to do so, they should not be permitted to stand by and make these payments for 11 years without expressing any expectation or making any demand for interest thereon, and then attempt to impose a new obligation upon the defendant, not provided for in the contract.

I would affirm the judgment, leaving the parties to their rights as expressed in the covenants of the contract as made, or as may be made in the future with respect to interest on such payments.

HENRIOD, C.J., concurs in the views expressed in the dissenting opinion of CROCKETT, J.

APPENDIX G

IN THE UTAH SUPREME COURT

Richard Madsen and Nancy Madsen, for themselves and all others similarly situated,

Plaintiffs, Appellants and Cross-appellees,

v.

Washington Mutual Bank fsb, (successor to Prudential Federal Savings and Loan Association),

Defendant, Appellee and Cross-appellant.

Case No. 20060597-SC

ORDER

(Filed Dec. 5, 2008)

This matter is before the court upon the Appellant's Petition for Rehearing, filed on October 15, 2008.

IT IS HEREBY ORDERED that pursuant to Rule 35 of the Utah Rules of Appellate Procedure the Petition for Rehearing is denied.

For the Court:

12-5-08 /s/ Matthew B Durrant
Date Matthew B. Durrant
Associate Chief Justice

APPENDIX H

Code of Federal Regulations

12

Banks and Banking

PART 300 TO END

Revised as of January 1, 1975

[LOGO]

CONTAINING
A CODIFICATION OF DOCUMENTS
OF GENERAL APPLICABILITY
AND FUTURE EFFECT

AS OF JANUARY 1, 1975

With Ancillaries

Published by
The Office of the Federal Register
National Archives and Records Service
General Services Administration

as a Special Edition of
the Federal Register

* * *

§ 541.5 Short-term savings account.

The term "short-term savings account" means a savings account in a Federal association which is to be withdrawn in less than twenty-four months from the date on which such account is opened, or a savings account in a Federal association established for the purpose of accumulating funds to pay taxes or

insurance premiums, or both, in connection with a loan on the security of a lien on real estate.

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§ 544.1 Issuance of charter.

(a) *Charter N.* Except as provided in paragraph (b) of this section and in § 544.2, the following form of charter, which shall be known as Charter N, will be issued on and after the effective date of the rules and regulations in this subchapter, upon approval by the Board of any petition for a charter for a Federal association pursuant to the provisions of subsections (a) or (i) of section 5 of Home Owners' Loan Act of 1933, as amended:

CHARTER N

1. *Corporate title.* The full corporate title of the Federal association hereby chartered is _____ Federal Savings and Loan Association _____.

2. *Office.* The home office shall be located at ___, in the County of _____, State of _____.

3. *Objects and powers.* The objects of the association are to promote thrift by providing a convenient and safe method for people to save and invest money and to provide for the sound and economical financing of homes; and, in the accomplishment of such objects, it shall have perpetual succession and power: (1) To act as fiscal agent of the United States when designated for that purpose by the Secretary of the Treasury, under such regulations as he may

prescribe, and shall perform all such reasonable duties as fiscal agent of the United States as he may require and to act as agent for any other instrumentality of the United States when designated for that purpose by any such instrumentality; (2) To sue and be sued, complain and defend in any court of law or equity; (3) To have a corporate seal, affixed by imprint, facsimile or otherwise; (4) To appoint afficers [sic] and agents as its business shall require, and allow them suitable compensation; (5) To adopt bylaws not inconsistent with the Constitution or laws of the United States and rules and regulations adopted thereunder and this charter; (6) To raise its capital, which shall be unlimited, by accepting payments on savings accounts representing share interests in the association; (7) To borrow money; (8) To lend and otherwise invest its funds; (9) To wind up and dissolve, merge, consolidate, convert, or reorganize; (10) To purchase hold, and convey real and personal estate consistent with its objects, purposes, and powers; (11) To mortgage or lease any real and personal estate and take such property by gift, devise, or bequest; and (12) To exercise all powers conferred by law. In addition to the foregoing powers expressly enumerated, this association shall have power to do all things reasonably incident to the accomplishment of its express objects and the performance of its express powers. It shall exercise its powers in conformity with all laws of the United States as they now are, or as they may hereafter be amended, and with all rules and regulations which are not in conflict with this charter, now or hereafter made thereunder.

4. *Members.* All holders of the association's savings accounts and all borrowers therefrom are members. In the consideration of all questions requiring action by the members of the association, each holder of a savings account shall be permitted to cast one vote for each $100, or fraction thereof, of the withdrawal value of his account. A borrowing member shall be permitted, as a borrower, to cast one vote, and to cast the number of votes to which he may be entitled as the holder of a savings account. No member, however, shall cast more than 50 votes. Voting may be by proxy. Any number of members present at a regular or special meeting of the members shall constitute a quorum. A majority of all votes cast at any meeting of members shall determine any question. The members who shall be entitled to vote at any meeting of the members shall be those owning savings accounts and borrowing members of record on the books of the association at the end of the calendar month next preceding the date of such meeting. The number of votes which each member shall be entitled to cast at any meeting of the members shall be determined from the books of the association as of the end of the calendar month next preceding the date of such meeting. Those who were members at the end of the calendar month next preceding the date of a meeting of members but who shall have ceased to be members prior to such meeting shall not be entitled to vote thereat. All savings accounts shall be nonassessable.

5. *Directors.* The association shall be under the direction of a board of directors of not less than 5 nor

more than 15, as fixed in the association's bylaws or, in the absence of any such bylaw provision, as from time to time expressly determined by resolution of the association's members. Each director of the association shall be a member of the association, and a director shall cease to be a director when he ceases to be a member. Directors of the association shall be elected by its members by ballot; *Provided*, That in the event of a vacancy in the directorate, including vacancies created by an increase in the number of directors, the board of directors may fill such vacancy, if the members of the association fail so to do, by electing a director to serve until the next annual meeting of the members. Directors shall be elected for periods of 3 years and until their successors are elected and qualified, but provision shall be made for the election of approximately one-third of the board of directors each year.

6. *Withdrawals.* The association shall have the right to pay the withdrawal value of its savings accounts at any time upon application therefor and to pay the holders thereof the withdrawal value thereof. Upon receipt of a written request from any holder of a savings account of the association for the withdrawal from such account of all or any part of the withdrawal value thereof, the association shall within 30 days pay the amount requested; *Provided*, That if the association is unable to pay all withdrawals requested at the end of 30 days from the date of such requests, it shall then pay all withdrawals requested in accordance with such methods and procedures as

to amounts and allotments of funds for such purposes as shall be provided in regulations made by the Federal Home Loan Bank Board in effect at the date of the request for withdrawal. Holders of savings accounts for which application for withdrawal has been made shall remain holders of savings accounts until paid and shall not become creditors.

7. *Redemption.* At any time sufficient funds are on hand, the association shall have the right to redeem, by lot or otherwise as the board of directors may determine, all or any part of any of its savings accounts on June 30 or December 31, by giving 30 days' notice of such redemption by registered mail addressed to the holder of each such savings account at his last address as recorded on the books of the association. The association may not redeem any of its savings accounts when there is an impairment of its capital or when it has any request for withdrawal which has been on file and unpaid for more than 30 days. The redemption price of each savings account redeemed shall be the full value thereof, as determined by the board of directors, but in no event shall the redemption price be less than the withdrawal amount of such savings account. If a savings account which is redeemed is entitled to participate in any reserve for bonus, the amount in such reserve for bonus which is properly allocable to such savings account shall be paid as part of the redemption price thereof. If any notice of redemption shall have been duly given, and if the funds necessary for such redemption shall have been set aside so as to be and to

continue to be available for that purpose, earnings upon such account shall cease to accrue from and after the date specified as the redemption date and all rights with respect to each such account shall forthwith, after such redemption date, terminate, except only the right of the holder of record of such savings account to receive the redemption price there of without earnings.

8. *Loans and investments.* The association may make any loan or investment authorized by statute and the rules and regulations made by the Home Loan Bank Board and in effect on August 15, 1949; it may make such additional loans and investments as may thereafter be authorized by amendments of the said rules and regulations.

9. *Power to borrow.* The association may borrow money in an aggregate amount not exceeding one-half of its capital; the amount which may be borrowed from sources other than a Federal home loan bank shall not exceed one-tenth of such capital. Notwithstanding the foregoing limitations, the association may, with prior approval by the Federal Home Loan Bank Board, borrow from a Federal home loan bank or from any Federal agency or instrumentality without limitation, upon such terms and conditions as may be required by such bank or agency. The association may pledge and otherwise encumber any of its assets to secure its debts.

10. *Reserves, surplus, and distribution of earnings.* The association shall maintain general reserves

for the sole purpose of meeting losses; such reserves shall include the reserve required for insurance of accounts. Any losses may be charged against general reserves. If and whenever the general reserves of the association are not equal to at least 10 percent of its capital, it shall, as of June 30 and December 31 of each year, credit to such reserves an amount equivalent to at least 5 percent of its net earnings for the 6 months' period, or such amount as may be required by the Federal Savings and Loan Insurance Corporation, whichever is greater, until such reserves are equal to at least 10 percent of the association's capital. As of June 30 and December 31 of each year, after payment or provision for payment of all expenses, credits to general reserves and such credits to surplus as the board of directors may determine, and provision for bonus on savings accounts as authorized by regulations made by the Federal Home Loan Bank Board, the board of directors of the association shall cause the remainder of the net earnings of the association for the 6 months' period to be distributed promptly on its savings accounts, ratably, as declared by the board of directors, to the withdrawal value thereof; in lieu of or in addition to such net earnings, any of the association's surplus funds may be likewise distributed. Such net earnings shall be credited to savings accounts or paid, as directed by the owner. All holders of savings accounts shall participate at the same rate and on the same basis in the distribution of earnings; *Provided*, That the association is not required to distribute earnings on short-term savings accounts or on accounts of $10 or less. Except as

provided above, earnings shall be declared on all savings accounts of record at the close of each such 6 months' period, on the withdrawal value of each such account at the beginning of the said 6 months' period, plus the payments made thereon during such period (less amounts withdrawn, and, for purposes or participation in earnings, deducted from the latest previous payments), computed at the declared rate for the time invested, determined as provided below. The date of investment shall be the date of actual receipt of such payments by the association, unless the board of directors fixes a date, not later than the tenth of the month, for determining the date of investment of payments on savings accounts or designated classes thereof. Payments, affected by such determination date, received by the association on or before such determination date shall receive earnings as if invested on the first of such month. Payments, affected by such determination date, received subsequent to such determination date shall receive earnings as if invested on the first of the next succeeding month. Notwithstanding any other provision of its charter, the association may distribute net earnings on its savings accounts on such other basis and in accordance with such other terms and conditions as may from time to time be authorized by regulations made by the Federal Home Loan Bank Board. All holders of savings accounts of the association shall be entitled to equal distribution of assets, pro rata to the value of their savings accounts, in the event of voluntary or involuntary liquidation, dissolution, or winding up of the association.

11. *Amendment of charter.* No amendment, addition, alteration, change, or repeal of this charter shall be made unless such proposal is made by the board of directors of the association, and submitted to and approved by the Federal Home Loan Bank Board, and is thereafter submitted to and approved by the members at a legal meeting. Any amendment, addition, alteration, change, or repeal so acted upon and approved shall be effective, if filed with and approved by the Federal Home Loan Bank Board, as of the date of the final approval of, or as fixed by, the members.

FEDERAL HOME LOAN BANK BOARD,

By _____
(Chairman)

Attest:

_____
(Secretary)

(b) *Charter K (rev.).* If expressly requested in the Petition for Charter, or in the Application for Conversion into a Federal association, the Board, in lieu of Charter N, will issue a Charter K (rev.), reading as follows:

CHARTER K. (REV.)

1. *Corporate title.* The full corporate title of the Federal association hereby chartered is _____ Federal Savings and Loan Association _____.

2. *Office.* The home office shall be located at ___, in the County of _____, State of _____.

3. *Objects and powers.* The objects of the association are to promote thrift by providing a convenient and safe method for people to save and invest money and to provide for the sound and economical financing of homes; and, in the accomplishment of such objects, it shall have perpetual succession and power: (1) To act as fiscal agent of the United States when designated for that purpose by the Secretary of the Treasury, under such regulations as he may prescribe, and shall perform all such reasonable duties as fiscal agent of the United States as he may require and to act as agent for any other instrumentality of the United States when designated, for that purpose by any such instrumentality; (2) To sue and be sued, complain and defend in any court of law or equity; (3) To have a corporate seal, affixed by imprint, facsimile or otherwise; (4) To appoint officers and agents as its business shall require, and allow them suitable compensation; (5) To adopt bylaws not inconsistent with the Constitution or laws of the United States and rules and regulations adopted thereunder and this charter; (6) To raise its capital, which shall be unlimited, by accepting payments on savings accounts representing share interests in the association; (7) To borrow money; (8) To lend and otherwise invest its funds; (9) To wind up and dissolve, merge, consolidate, convert, or reorganize; (10) To purchase, hold, and convey real and personal estate consistent with its objects, purposes, and powers; (11) To mortgage or lease any real and personal estate and take such property by gift, devise, or bequest; and (12) To exercise all powers conferred by

law. In addition to the foregoing powers expressly enumerated, this association shall have power to do all things reasonably incident to the accomplishment of its express objects and the performance of its express powers. It shall exercise its powers in conformity with all laws of the United States as they now are, or as they may hereafter be amended, and with all rules and regulations which are not in conflict with this charter now or hereafter made thereunder.

4. *Members.* All holders of the association's savings accounts and all borrowers therefrom are members. In the consideration of all questions requiring action by the members of the association, each holder of a savings account shall be permitted to cast one vote for each $100, or fraction thereof, of the withdrawal value of his account. A borrowing Member shall be permitted, as a borrower, to cast one vote, and to cast the number of votes to which he may be entitled as the holder of a savings account. No member, however, shall cast more than 50 votes. Voting may be by proxy. Any number of members present at a regular or special meeting of the members shall constitute a quorum. A majority of all rates cast at any meeting of members shall determine any question. The members who shall be entitled to vote at any meeting of the members shall, be those owning savings accounts and borrowing members of record on the books of the association at the end of the calendar month next preceding the date of such meeting. The number of votes which each member shall be entitled to cast at any meeting of the members shall be

determined from the books of the association as of the end of the calendar month next preceding the date of such meeting. Those who were members at the end of the calendar month next preceding the date of a meeting of members but who shall have ceased to be members prior to such meeting shall not be entitled to vote thereat. All savings accounts shall be non-assessable.

5. *Directors.* The association shall be under the direction of a board of directors of not less than 5 nor more than 15, as fixed in the association's bylaws or, in the absence of any such bylaw provision, as from time to time expressly determined by resolution of the association's members. Each director of the association shall be a member of the association, and a director shall cease to be a director when he ceases to be a member. Directors of the association shall be elected by its members by ballot: *Provided*, That in the event of a vacancy in the directorate, including vacancies created by an increase in the number of directors, the board of directors may fill such vacancy, if the members of the association fail so to do, by electing a director to serve until the next annual meeting of the members. Directors shall be elected for periods of 3 years and until their successors are elected and qualified, but provision shall be made for the election of approximately one-third of the board of directors each year.

6. *Withdrawals.* The association shall have the right to pay the withdrawal value of its savings accounts at any time upon application therefor and to

pay the holders thereof the withdrawal value thereof. Upon receipt of a written request from any holder of a savings account of the association for the withdrawal from such account of all or any part of the withdrawal value thereof, the association shall within 30 days pay the amount requested; *Provided*, That if the association is unable to pay all withdrawals requested at the end of 30 days from the date of such requests, it shall then proceed in the following manner while any withdrawal request remains unpaid for more than 30 days:

Withdrawal requests shall be paid in the order received and if any holder of a savings account or accounts has requested the withdrawal of more than $1,000, he shall be paid $1,000 in order when reached and his withdrawal request shall be charged with such amount as paid and shall be renumbered and placed at the end of the list of withdrawal requests, and thereafter, upon again being reached, shall be paid a like amount, but not exceeding the withdrawal value of his savings account, and until such withdrawal request shall have been paid in full, shall continue to be so paid, renumbered, and replaced at the end of the withdrawal requests on file: *Provided*, That when any such request is reached for payment, the association shall so advise the holder of such savings account by registered mail to his last address as recorded on the books of the association and, unless such holder shall apply in person or in writing for the payment of such withdrawal request within 30 days from the date of the mailing of such notice, no

payment on account of such withdrawal request shall be made and such request shall be cancelled: *And provided further*, That the board of directors shall have absolute right to pay on an equitable basis an amount not exceeding $200 to any holder of a savings account or accounts in any calendar month and without regard to any other provision of this section.

When the association is unable to pay all withdrawal requests within a period not exceeding 30 days from the date of receipt of written request therefor it shall allot to the payment of such requests the remainder of the association's receipts from all sources after deducting from total receipts appropriate amounts for expenses, required payments on indebtedness, earnings distributable in cash to holders of savings accounts, and a fund for general corporate purposes equivalent to not more than 20 percent of the association's receipts from holders of its savings accounts and from its borrowers. Holders of savings accounts for which application for withdrawal has been made shall remain holders of savings accounts until paid and shall not become creditors.

7. *Redemption*. At any time sufficient funds are on hand, the association shall have the right to redeem, by lot or otherwise as the board of directors may determine, all or any part of any of its savings accounts on June 30 or December 31, by giving 30 days' notice of such redemption by registered mail addressed to the holder of each such savings account at his last address as recorded on the books of the association. The association may not redeem any of

its savings accounts when there is an impairment of its capital or when it has any request for withdrawal which has been on file and unpaid for more than 30 days. The redemption price of each savings account redeemed shall be the full value thereof, as determined by the board of directors, but in no event shall the redemption price be less than the withdrawal amount of such savings account. If a savings account which is redeemed is entitled to participate in any reserve for bonus, the amount in such reserve for bonus which is properly allocable to such savings account shall be paid as part of the redemption price thereof. If any notice of redemption shall have been duly given, and if the funds necessary for such redemption shall have been set aside so as to be and to continue to be available for that purpose, earnings upon such account shall cease to accrue from and after the date specified as the redemption date and all rights with respect to each such account shall forthwith, after such redemption date, terminate, except only the right of the holder of record of such savings account to receive the redemption price thereof without earnings.

8. *Loans and investments.* The association may make any loan or investment authorized by statute and the rules and regulations made by the Home Loan Bank Board and in effect on August 15, 1949; it may make such additional loans and in-vestments as may thereafter be authorized by amendments of the said rules and regulations.

9. *Power to borrow.* The association may borrow money in an aggregate amount not exceeding one-half of its capital; the amount which may be borrowed from sources other than a Federal home loan bank shall net exceed one-tenth of such capital. Notwithstanding the foregoing limitations, the association may, with prior approval by the Federal Home Loan Bank Board, borrow from a Federal home loan bank or from any Federal agency or instrumentality without limitation, upon such terms and conditions as may be required by such bank or agency. The association may pledge and otherwise encumber any of its assets to secure its debts.

10. *Reserves, surplus, and distribution of earnings.* The association shall maintain general reserves for the sole purpose of meeting losses; such reserves shall include the reserve required for insurance of accounts. Any losses may be charged against general reserves. If and whenever the general reserves of the association are not equal to at least 10 percent of its capital, it shall, as of June 30 and December 31 of each year, credit to such reserves an amount equivalent to at least 5 percent of its net earnings for the 6 months' period, or such amount as may be required by the Federal Savings and Loan Insurance Corporation, whichever is greater, until such reserves are equal to at least 10 percent of the association's capital. As of June 30 and December 31 of each year, after payment or provision for payment of all expenses, credits to general reserves and such credits to surplus as the board of directors may determine, and

provision for bonus on savings accounts as authorized by regulations made by the Federal Home Loan Bank Board, the board of directors of the association shall cause the remainder of the net earnings of the association for the 6 months' period to be distributed promptly on its savings accounts, ratably, as declared by the board of directors, to the withdrawal value thereof; in lieu of or in addition to such net earnings, any of the association's surplus funds may be likewise distributed. Such net earnings shall be credited to savings accounts or paid, as directed by the owner. All holders of savings accounts shall participate at the same rate and on the same basis in the distribution of earnings: *Provided*, That the association is not required to distribute earnings on short-term savings accounts or on accounts of $10 or less. Except as provided above, earnings shall be declared on all savings accounts of record at the close of each such 6 months' period, on the withdrawal value of each such account at the beginning of the said 6 months' period, plus the payments made thereon during such period (less amounts withdrawn, and, for purposes of participation in earnings, deducted from the latest previous payments), computed at the declared rate for the time invested, determined as provided below. The date of investment shall be the date of actual receipt of such payments by the association, unless the board of directors fixes a date, not later than the tenth of the month, for determining the date of investment of payments on savings accounts or designated classes thereof. Payments, affected by such determination date, received by the association on or

before such determination date, shall receive earnings as if invested on the first of such month. Payments, affected by such determination date, received subsequent to such determination date, shall receive earnings as if invested on the first of the next succeeding month. Notwithstanding any other provision of its charter, the association may distribute net earnings on its savings accounts on such other basis and in accordance with such other terms and conditions as may from time to time be authorized by regulations made by the Federal Home Loan Bank Board. All holders of savings accounts of the association shall be entitled to equal distribution of assets, pro rata to the value of their savings accounts, in the event of voluntary or involuntary liquidation, dissolution, or winding up of the association.

11. *Amendment of charter.* No amendment, addition, alteration, change, or repeal of this charter shall be made unless such proposal is made by the board of directors of the association, and submitted to an approved by the Federal Home Loan Bank Board, and is thereafter submitted to an approved by the members at a legal meeting. Any amendment, addition, alteration, change, or repeal so acted upon and approved shall be effective, if filed with and approved by the Federal Home Loan Bank Board, as of the date of the final approval of, or as fixed by, the members.

H20

FEDERAL HOME LOAN BANK BOARD,

By _____
(Chairman)

Attest:

_____
(Secretary)

Code of Federal Regulations

12

Banks and Banking

PART 300 TO END

Revised as of January 1, 1976

[LOGO]

CONTAINING
A CODIFICATION OF DOCUMENTS
OF GENERAL APPLICABILITY
AND FUTURE EFFECT

AS OF JANUARY 1, 1976

With Ancillaries

Published by
The Office of the Federal Register
National Archives and Records Service
General Services Administration

as a Special Edition of
the Federal Register

* * *

§ 545.6-11 Loan contract.

* * *

(c) *Payment of interest on escrow accounts.* A Federal association which makes a loan on or after June 16, 1975 on the security of a single-family dwelling occupied or to be occupied by the borrower (except such a loan for which a bona fide commitment was made before that date) shall pay interest on any escrow account maintained in connection with such a loan (1) if there is in effect a specific statutory provision or provisions of the State in which such dwelling is located by or under which State-chartered savings and loan associations, mutual savings banks and similar institutions are generally required to pay interest on such escrow accounts, and (2) at not less than the rate required to be paid by such State-chartered institutions but not to exceed the rate being paid by the Federal association in its regular accounts (as defined in § 526.1 of this chapter). Except as provided by contract, a Federal association shall have no obligation to pay interest on escrow accounts apart from the duties imposed by this paragraph.

APPENDIX I

Hansen, Bradshaw, Malmrose & Erickson
A Professional Corporation
CERTIFIED PUBLIC ACCOUNTANTS

559 West 500 South
Bountiful, Utah 84010
801-296-0200
Fax 801-296-1218

March 1, 2002

[Additional CPA Names Omitted In Printing]

(FILED MAR 4, 2002)

Honorable Michael K. Burton
Third Judicial District Court
Salt Lake County, State of Utah

Dear Judge Burton:

This letter is our Report to the Court as required by the Court in its Order dated January 2, 2002. This Order specified the following:

> The Master shall, within 60 days of this order, produce to the Court a Report giving the Master's final statistical calculation of aggregate class damages. Furthermore for purposes of this report, if the mailing address and the property address are identical on the Mortgage Loan Master Reference Card (sample attached), the Master shall assume that such loans involve "primary residence", as that terms is used in prior Orders of the Court.

To accomplish this objective I met with Brad Slack at Washington Mutual to review the data base that he had prepared of the loan origination cards. This data base was prepared by Mr. Slack and other Washington Mutual Bank employees under his direction, as outlined in his August 7, 2000 affidavit filed with the Court. This process resulted in a data base of 14,482 loan cards. It should be noted that I have only performed a limited amount of testing of this data base, primarily in obtaining a sample of 50 loan cards to respond to plaintiff counsel's request of December 27, 2000. I have not yet performed testing to determine if all loan cards have been properly segregated between class members and non-members of the class. Based on the limited testing I have performed and based on my meetings and discussions with Mr. Slack, I have seen no evidence that the process of segregating the loan cards and developing the data base was not performed with due care.

The data base includes information regarding the mailing address of the borrower, as well as the property address as listed on each loan origination card. We requested that Mr. Slack print the entire data base and mark each borrower name where the loan address and property address did not agree. In performing this task, he also noted a third group of borrowers; those where it is not possible to determine if the mailing address and the property address are the same. There are two primary reasons for this classification; the first is when the property address is listed on the card but the mailing address is a P.O.

box, the second is when a legal description of the property is listed as the property address. Mr. Slack marked this third category as well on the printout of the database.

After Mr. Slack completed the process of marking the data base printout for the three different categories, we obtained the printout from him. We tested the accuracy of his work by reviewing the printout and looking for any items which appeared to be improperly classified, based on the information listed. We found a small number of exceptions, and met with Mr. Slack to discuss the exceptions. He then made the appropriate corrections on the printout.

We then met again with Mr. Slack to sort the data base into the three categories:

1. Borrowers where the mailing address and property address agree.

2. Borrowers where the mailing address and property address did not agree.

3. Borrowers where it was indeterminable if the mailing address and property address agree.

As noted above, there were 14,482 total loans in the data base. This sorting process identified 10,796 loans in category 1, 3,192 loans in category 2, and 494 loans in category 3. Of the 10,796 loans in category 1 where the addresses match, there are 1,249 loans which are duplicated on the listing. Of the 494 loans in category 3, 30 are duplicate loans within the listing

and an additional 57 are duplicates when compared to category 1. Duplication occurs primarily from assumption of the same loan by one or more subsequent borrowers. We considered whether duplicate loan numbers should be included in the estimate of aggregate damages and concluded they should be excluded. We arrived at this conclusion after considering the methodology used by Prudential in conducting its sample in 1993, from which we use data as described below in developing our estimate of aggregate damages. After subtracting the duplicate borrowers, the adjusted total of category 1 loans (where the property and mailing address match) was 9,547.

As discussed in our Report to the Court dated December 31, 1996, Prudential used the December 31, 1972 mortgage loan microfiche records as the population for its sample. For each of the 400 loans selected in its sample, Prudential obtained the annual statement summaries for the loan for each year from 1971 to 1979. The damage calculations were performed for the entire period the loan was outstanding from 1971 to 1979, whether the loan was assumed or not. Prudential's damage calculations for its sample were on a per loan basis, rather than per individual borrower.

As noted in our December 31, 1996 Report to the Court, the amount of damages for the 227 potential class loans from the sample totaled 23,875.69, or an average of $105.18 per class member or loan. For the purposes of this Report as directed by the Court, we believe this per loan sample average is meaningful

and can be used to develop our estimate of aggregate damages, as follows:

Number of loans where property address and mailing address agree	9,547
Average damages per loan, from 1993 sample, for period March 3, 1971 to June 30, 1979	$ 105.18
Estimate of aggregate damages	$1,004,153

This aggregate damage estimate excludes any judgement interest subsequent to June 30, 1979.

If the category 3 or indeterminable loans were included in the above estimate, they would increase the estimate by a maximum of $42,808 if all of the non-duplicate total of 407 loans were found to be category 1 loans.

As previously noted, the completeness and accuracy of the data base has not been extensively tested. I would point out that the process used by Washington Mutual to develop this data base resulted in 9,547 loans identified, as described above. Our December 31, 1996 report to the Court arrived at an estimated 9,648 class members, based on the 1993 sample performed. The sample estimate of 9,648 is a close approximation of the 9,547 arrived at by individual examination of loan cards by Washington Mutual to prepare the data base, and provides additional evidence of the overall reasonableness of the class member size. While the exact number of class members

may not be known at the present time, I believe we have a reasonable estimate of class member loans that can in turn be used to provide an overall estimate of aggregate damages.

The following are certain of the statistical parameters used by Prudential in their 1993 sample of 400 loans:

Population Estimate:

n	100
X-BAR	94.96
N	16,941
X-HAT	1,608,639

Confidence Interval Data:

Standard Deviation	118.42
Finite Correction Factor	0.99704
Standard Error	200,030
Reliability Level (Two-sided)	95%
Confidence Coefficient	1.96
Precision	392,059

Please contact me regarding any questions concerning the information in this letter.

Respectfully submitted,

/s/ Edwin Erickson
Edwin L. Erickson, CPA

ELE:cp

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(3)

Supreme Court, U.S.
FILED
MAY 4 - 2009
OFFICE OF THE CLERK

No. 08-1098

IN THE

Supreme Court of the United States

RICHARD MADSEN and NANCY MADSEN,

Petitioners,

v.

JP MORGAN CHASE BANK, N.A.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF UTAH

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

Whether Petitioners' desire to send "a stern warning to lawyers and judges, throughout the land, that issues of federal preemption should be heard in the beginning of a case, and not delayed until the middle or the end of the case" presents a compelling reason to grant the Petition.

Whether Petitioners have presented a compelling reason to grant the Petition when no conflict exists between the Utah Supreme Court decision disposing of Petitioners' state law claim on grounds of federal preemption, and the earlier decision of the United States Court of Appeals for the Tenth Circuit which remanded the case to state court for lack of federal question jurisdiction.

CORPORATE DISCLOSURE STATEMENT

Respondent JP Morgan Chase Bank, N.A., the successor in interest to Washington Mutual Bank, fsb, has the following parent corporation: JP Morgan Chase Co. JP Morgan Chase Co. is the only publicly held company that owns 10% or more of the stock of JP Morgan Chase Bank, N.A.

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INTRODUCTION

The Petition should be denied because it presents no compelling reason to grant a Writ of Certiorari.

Petitioners primarily argue that certiorari should be used to "give a stern warning to lawyers and judges, throughout the land" that federal preemption issues should be raised at the beginning of a case. However, the preemption issues were, in fact, raised throughout this case, and in any event, Petitioners have not presented any compelling reason why certiorari should be used for this purpose. Second, contrary to Petitioners' argument, the Tenth Circuit Court of Appeals' 1980 decision in this case does not conflict with the Utah Supreme Court's 2008 decision in this case, and therefore there is no conflict for this Court to resolve.

In addition, the issues raised by this case are not likely to recur or have significance beyond this case. Petitioners' claim relates to mortgage payments made from 1971 (four years before this suit was filed) and 1979 (when state legislation was enacted). The form of trust deed on which this claim is based has not been used by Prudential since 1973. Petitioners' claim was dismissed by the Utah Supreme Court based on federal regulations in effect in the 1970s, which have since been amended. The Utah Supreme Court's ruling is correct and based on the unique facts of this case. Petitioners' contention that the ruling is incorrect is not a compelling reason to grant certiorari. In any event, the issues raised are not likely to recur or have relevance beyond this case. Thus, there is no compelling reason to grant certiorari.

STATEMENT OF THE CASE

1. In 1975, Nancy and Richard Madsen ("Madsens")[1] sued Prudential Federal Savings & Loan Association ("Prudential")[2] seeking to recover interest or earnings on amounts paid into a reserve account (or budget account) maintained to pay taxes and insurance on the property securing their mortgage loan owed to Prudential.

2. In 1976, the trial court granted Prudential's Motion for Summary Judgment dismissing Madsens' claims, and denied Madsens' Motion for Partial Summary Judgment.[3]

---

1. Richard Madsen died during the pendency of this case and the trial court modified the case caption to reflect Nancy Madsen as plaintiff. As was the practice in the lower courts, Respondent will continue to refer to the Petitioner in the plural as "Madsens."

2. Prudential was eventually acquired by Washington Mutual Bank, fsb, and the trial court modified the case caption to reflect Washington Mutual as the successor to Prudential. Petitioners have identified the Respondent as JP Morgan Chase Bank, N.A. As has been the practice in the lower courts, Respondent will continue to refer to the Respondent as Prudential.

3. In the mid-1970's, numerous cases were filed throughout the country seeking interest on mortgage loan reserve accounts. The overwhelming majority of reported decisions rejected the various theories presented by the plaintiffs. *See, e.g., Gibson v. First Fed. Sav. & Loan Ass'n*, 364 F. Supp. 614 (E.D. Mich. 1973), *aff'd*, 504 F.2d 826 (6th Cir. 1974); *Stavrides v. Mellon Nat'l Bank*, 353 F. Supp. 1072 (W.D. Pa. 1973), *aff'd*, 487 F.2d 953 (3d Cir.

(Cont'd)

3. Madsens appealed, and the Utah Supreme Court reversed and remanded. *See Madsen v. Prudential Fed. Sav. & Loan Ass'n*, 558 P.2d 1337 (Utah 1977) (hereafter "*Madsen I*"). (Appendix F to Petition for Writ of Certiorari.)

4. In 1977, after remand, Madsens filed their Second Amended Complaint. Prudential asserted federal preemption as a defense and removed the case to the United States District Court for the District of Utah.

(Cont'd)

1973); *Manchester Gardens, Inc. v. Great West Life Assurance Co.*, 205 F.2d 872 (D.C. Cir. 1953); *Umdenstock v. Am. Mortgage & Inv. Co.*, 363 F. Supp. 1375 (W.D. Okla. 1973); *Zelickman v. Bell Fed. Sav. and Loan Ass'n*, 275 N.E.2d 300 (Ill. App. Ct. 1971); *Brooks v. Valley Nat'l Bank* ("*Brooks I*"), 539 P.2d 958 (Ariz. Ct. App. 1975), *vacated, Brooks v. Valley Nat'l Bank* ("*Brooks II*"), 548 P.2d 1166 (Ariz. 1976); *Surrey Strathmore Corp. v. Dollar Sav. Bank of New York*, 325 N.E.2d 527 (N.Y. 1975); *Richman v. Security Sav. & Loan Ass'n*, 204 N.W.2d 511 (Wis. 1973); *Durkee v. Franklin Sav. Ass'n*, 309 N.E.2d 118 (Ill. App. Ct. 1974); *Yudkin v. Avery Fed. Sav. Loan Ass'n*, 507 S.W.2d 689 (Ky. Ct. App. 1974); *Kinee v. Abraham Lincoln Fed. Sav. & Loan Ass'n*, 365 F. Supp. 975 (E.D. Pa. 1973); *Petherbridge v. Prudential Sav. & Loan Ass'n*, 79 Cal. App. 3d 5059 (Cal. Ct. App. 1978); *Kronisch v. Howard Sav. Inst.*, 392 A.2d 178 (N.J. Super. Ct. App. Div. 1978); *Tierney v. Whitestone Sav. & Loan Ass'n*, 373 N.Y.S.2d 724 (N.Y. App. Div.1975); *Tucker v. Pulaski Fed. Sav. & Loan Ass'n*, 481 S.W.2d 725 (Ark. 1972); *Cale v. Am. Nat'l Bank*, 370 Ohio Misc. 56 (1973); *Carpenter v. Suffolk Franklin Sav. Bank* ("*Carpenter II*"), 346 N.E.2d 892 (Mass. 1976). *Kronisch*, *Carpenter II* and *Brooks II* summarize the history of the litigation at that time. *But see Derenco v. Benjamin Franklin Fed. Sav. & Loan Ass'n*, 557 P.2d 427 (Ore. 1978) and *Madsen v. Prudential Fed. Sav. & Loan Ass'n*, 558 P.2d 1337 (Utah 1977).

5. On April 19, 1979, the United States District Court for the District of Utah granted summary judgment in favor of Prudential, dismissing Madsens' claims on the basis that federal regulations preempted Madsens' state law claim for interest on the reserve account.

6. Madsens appealed the federal court ruling. On appeal, the Tenth Circuit Court of Appeals reversed and remanded, not on the merits but solely for lack of federal jurisdiction because a "federal question" was not presented on the face of the complaint but existed only as a defense. Prudential filed a Petition for Writ of Certiorari to review this decision and Madsens objected to the Petition. The Petition was denied. *See Madsen v. Prudential Fed. Sav. & Loan Ass'n*, 635 F.2d 797 (10th Cir. 1980), *cert. denied*, 451 U.S. 1018 (1981) (hereafter "*Madsen II*"). (Appendix E to Petition for Writ of Certiorari.)

7. After remand to the state court, Madsens filed their Substitute Third Amended Complaint (Class Action) (the present complaint) on October 14, 1981. The complaint alleged claims of unjust enrichment and accounting, fraud and statutory damages. The complaint did not allege a breach of contract claim.

8. In 1985, on the eve of trial, the trial court denied Prudential's motion for summary judgment which argued that Madsens' claims were preempted by federal regulations.

9. In 1985, trial was held on Madsens' individual claim only, with all class issues being reserved.

10. On March 22, 1990, the trial court entered Findings of Fact and Conclusions of Law on Madsens' individual claim only. Madsens were awarded damages of $134.70, plus interest at 10% per annum from the date of trial to the entry of judgment. The court fixed the damage recovery period from March 3, 1971 (four years before the complaint was filed) to June 30, 1979 (the date after which Utah Code Ann. §§ 7-17-1 to -10 became effective and the date on which Prudential no longer required reserve payments on most trust deeds, including Madsens'). (Appendix C to Petition for Writ of Certiorari.) By Memorandum Decision dated January 30, 1998, the trial court ruled that the granting of interest from the date of the trial to the date of entry of judgment was erroneous.

11. From December 1996 (when the judge who presided over the trial retired) to June 2006 (the time of entry of final judgment as to the class), Madsens filed numerous motions, including over thirty motions challenging the class definition, challenging the damages calculation, seeking to expand the damages period adopted by the trial court, or seeking removal of the Special Master, all of which were denied.

12. From December 1996 to the time of entry of final judgment, Madsens filed nine petitions for interlocutory appeal or writs of mandamus, all of which were denied.

13. Final judgment was entered in this matter on June 1, 2006. Madsens filed a Notice of Appeal on June 28, 2006. Prudential filed its Notice of Cross Appeal on July 12, 2006.

14. On September 23, 2008, the Utah Supreme Court reversed the trial court and dismissed Madsens' claim on the grounds that federal regulations governing Prudential preempted Madsens' state law claim for unjust enrichment and accounting. *See Madsen v. Washington Mut. Bank, fsb*, 199 P.3d 898 (Utah 2008) (hereafter "*Madsen IV*"). (Appendix A to Petition for Writ of Certiorari.)

REASONS FOR DENYING THE PETITION

THE WRIT SHOULD BE DENIED BECAUSE THERE IS NO COMPELLING REASON TO GRANT REVIEW.

Rule 10 of the Rules of the Supreme Court of the United States provides that a "petition for a writ of certiorari will be granted only for compelling reasons." In the present case, the Petition should be denied because there is no such compelling reason.

First, Madsens state that certiorari should be granted "so that this Court can give a stern warning to lawyers and judges, throughout the land, that issues of federal preemption should be heard in the beginning of a case, and not delayed until the middle or the end of the case." (Petition at 7) (emphasis omitted.) However, the desire to give "lawyers and judges" a "stern warning" about the timing of issues in a case is not a "compelling reason[]" to grant certiorari. Second, contrary to Madsens' assertion, the 1980 decision of the Tenth Circuit Court of Appeals in this case does not conflict with the 2008 decision of the Utah Supreme Court.

For these reasons, this Court should decline to exercise its discretionary power to accept this case for review, as it does not present any compelling issue that might be worthy of review by the United States Supreme Court. Each of these points is addressed in turn.

A. Certiorari is Not Necessary to Send a Message to "Lawyers and Judges" About Managing Cases.

Madsens' primary argument in support of their Petition is that "certiorari should be granted, so that this Court can give a *stern warning* to lawyers and judges, throughout the land, that issues of federal preemption should be heard in the beginning of a case, and not delayed until the *middle* or the *end* of the case." (Petition at 7.) However, giving a "stern warning" about how a case should proceed simply is not a compelling reason to grant certiorari. In any event, federal preemption issues were raised and heard at early stages in this proceeding. (*See* Statement of the Case *supra* at ¶¶ 5 and 8.) Final ruling on the issue of federal preemption necessarily occurred on final appeal, after entry of judgment on all issues.

More importantly, this case presents no compelling reason for review because the case relates to mortgage payments made in the 1970s, involving mortgage forms no longer in use and regulations since amended.[4] Thus,

4. The 1975 federal regulation which governs the escrow payments made in this case in the 1970s, then found at 12 C.F.R. § 545.6-11 (1976), was recodified in 1979 at 12 C.F.R. § 548.3 (1979), and then substantially amended in 1983 as a result of the Garn-St. Germain Depository Institutions Act of 1982. *See* 48 Fed. Reg. 23032 (May 23, 1983).

the issues are not likely to recur or have significance beyond this case. *Cf. Simon & Schuster, Inc. v. Members of the New York State Crime Victims Bd.*, 502 U.S. 105, 115 (1991) (granting certiorari because "the issue is significant and likely to recur"). Further, this case does not involve any issue of general importance, *cf. Chrysler Corp. v. Brown*, 441 U.S. 281, 289-90 (1979) (granting certiorari because of a conflict in the circuits "and the general importance of these . . . cases"), nor does it involve a conflict among circuits, *cf. Dean v. United States*, No. 08-5274, 2009 WL 1138892, at *2 (U.S. Apr. 29, 2009) (granting certiorari "to resolve th[e] conflict" among Circuits). *Cf. also Corley v. United States*, 129 S. Ct. 1558, 1566 (2009) (granting certiorari "to resolve a division in the Circuit Courts on the reach of [a federal statute]"); *Grutter v. Bollinger*, 539 U.S. 306, 322 (2003) (granting certiorari "to resolve the disagreement among the Court of Appeals on a question of national importance . . .").

B. The Ruling of the Utah Supreme Court (*Madsen IV*) Does Not Conflict with the Ruling of the Tenth Circuit (*Madsen II*).

Madsens' Petition asserts that there is a conflict between the ruling of the United States Court of Appeals for the Tenth Circuit ("*Madsen II*") and the final ruling of the Utah Supreme Court ("*Madsen IV*"). There is no such conflict.

Madsens erroneously argue that the Tenth Circuit Court of Appeals in *Madsen II* "concluded that there was a contract," while the "Utah Supreme Court concluded that there was no contract." (Petition at 8.)

This is incorrect. The Tenth Circuit held that no federal question jurisdiction existed, and therefore reversed summary judgment that had been granted in Prudential's favor. The Tenth Circuit did not rule on the substance of Madsens' claim or any of Prudential's defenses. *See Madsen v. Prudential Fed. Sav. & Loan Ass'n*, 635 F.2d 797, 801 (10th Cir. 1980) ("*Madsen II*"). The Utah Supreme Court ruled that Madsens' claim for unjust enrichment and accounting was barred by federal regulations. *See Madsen v. Washington Mut. Bank, fsb*, 199 P.3d 898, 905-07 (Utah 2008) ("*Madsen IV*").

In any event, the assertion in Madsens' Petition that either *Madsen II* or *Madsen IV* made erroneous factual findings or misapplied the law is not a compelling reason for review. *See* United States Supreme Court Rule 10 ("A petition for a writ of certiorari is rarely granted when the asserted error consists of erroneous factual findings or the misapplication of a properly stated rule of law.")

1. The Tenth Circuit (*Madsen II*) held that no federal question jurisdiction existed.

After the first appeal in this case in 1977 in which the Utah Supreme Court remanded the case to the trial court, Madsens amended their complaint. Thereafter, Prudential removed the case to federal court, alleging that the relief requested arose under and was controlled by preemptive federal law. Madsens moved to remand the case based on a lack of federal question jurisdiction. The United States District Court for the District of Utah denied the Madsens' motion to remand and granted summary judgment in Prudential's favor on the basis of preemption. On appeal, Madsens argued that

the federal court lacked jurisdiction. The Tenth Circuit reversed, and remanded the case to state court based on a lack of federal question jurisdiction. *Madsen II* at 799-800.

The issue at the Tenth Circuit was whether the federal court had jurisdiction of the removed action. *Id.* at 800. The Tenth Circuit explained that for a cause of action to "arise under" federal law "the federal controversy must be 'disclosed upon the face of the complaint, unaided by the answer or by the petition for removal.'" *Id.* at 800-01 (citations omitted). Thus, federal question jurisdiction existed, according to the Tenth Circuit, only if Madsens' complaint raised the federal question, not if Prudential's defenses raised a federal question. *Id.* at 801. Applying these principles, the Tenth Circuit found that there was no federal question jurisdiction, explaining:

> Although construction of the federal regulation cited by Prudential may be relevant to the defense Prudential asserts, *i.e.*, that section 545.6-11(c) does not require payment of interest, the meaning of the regulation is absolutely irrelevant to the Madsens' theory of recovery. Because the Madsens have predicated their suit upon rights created under state law, the fact that federal regulations may create a defense to recovery on such a claim is immaterial to a finding of federal question jurisdiction.

Id. at 801.

Thus, the Tenth Circuit decision in *Madsen II* did not reach the substance of any federal defense raised by Prudential, but rather expressly acknowledged that those defenses were yet to be heard.

Madsens argue that the statement by the Tenth Circuit in *Madsen II* that "state law is applicable in determining whether Prudential contracted to pay interest" is a holding by that court that a contract to pay interest existed. (Petition at 8.) This is not correct. The Tenth Circuit language cited by Madsens was

> presented in response to Prudential's argument that the controversy required the court to apply federal common law in determining whether the parties had entered into a contract for the payment of interest. . . . The passage cited by the Madsens is the Tenth Circuit's acknowledgment that under the explicit terms of 12 C.F.R. § 545.6-11(c), lenders' interest obligations could be varied by contract between private parties. The question of whether such a private contract had been created is, as the Tenth Circuit concluded, governed by state law.

Madsen IV at 906-07.

Therefore, the Tenth Circuit in *Madsen II* did not hold that a contract to pay interest existed, but rather dismissed for lack of federal question jurisdiction, and in doing so, stated that state law contract issues, and federal preemption defenses, were yet to be decided.

As a result, Madsens are incorrect in asserting that the Tenth Circuit "concluded that there was a contract" (Petition at 8) and, hence, the Tenth Circuit's decision does not conflict with the decision of the Utah Supreme Court.

2. The Utah Supreme Court (*Madsen IV*) correctly held that Madsens' claim is barred by federal regulations in effect at the time Madsens' claim arose.

The Utah Supreme Court correctly held that no contract existed for the payment of interest and thus Madsens' claims are barred by federal regulations governing Prudential (as a federal savings and loan association). The specific regulation in effect at the relevant time provided that, except as provided by statute or by contract, a federal association "shall have no obligation to pay interest on escrow accounts." *Madsen IV* at 904 (*citing* 12 C.F.R. § 545-6-11(c)). Under that regulation, Prudential had no obligation to pay interest on the Madsens' mortgage escrow account because no contract requiring the payment of interest existed.

Madsens' claim was not for breach of contract, but rather for "Accounting and Unjust Enrichment." Indeed, Madsens' complaint does not allege a written contract to pay interest, but rather argues the effect of a common law pledge. The 1977 decision in *Madsen I* confirmed that the Madsens' claim is not based on a contract, but rather that it "is predicated on the theory that the monthly budget payments . . . constitute a common law pledge." *Madsen I* at 1339.

That common law pledge, if it existed, arose out of pledge language contained in the trust deed used by Prudential for Madsens' loan, but that trust deed "did not contain any provision requiring Prudential to pay interest or profits on the budget payments." *Madsen IV* at 900. Rather, "Madsens argued that Prudential was unjustly enriched because the budget payments were held as a pledge and the common law required Prudential, as pledgee, to account for any profits earned through the use of the pledge." *Id.* As the Utah Supreme Court correctly explained, "[i]n this case, however, the Madsens have not claimed that a provision of the contract obligated Prudential to pay interest. Indeed, there is no such provision." *Id.* at 907.

Based on the then applicable regulations, and Madsens' claim, the Utah Supreme Court correctly concluded that "Prudential had no obligation to pay interest to the Madsens absent a state statute or contractual obligation to the contrary. The Madsens' accounting claim is not founded on a contract or statute." *Id.* at 904.

Thus, Madsens did not allege a written contract to pay interest, but rather argued the effect of a common law pledge, and there is no inconsistency between the decision of the Tenth Circuit in *Madsen II* and the decision of the Utah Supreme Court in *Madsen IV*.

C. The Ruling of the Utah Supreme Court Does Not Conflict with *Altria*.

Finally, Madsens incorrectly argue that the Utah Supreme Court's decision in *Madsen IV* conflicts with *Altria Group, Inc. v. Good*, 129 S. Ct. 538 (2008), because, Madsens contend, "when the text of a pre-emption clause is susceptible of more than one plausible reading, courts ordinarily accept the reading that disfavors pre-emption." (Petition at 9, 10.) However, Madsens fail to identify any express preemption clause applicable to this case that could be "susceptible of more than one plausible reading." Instead, Madsens argue only that there is a factual conflict between *Madsen II* and *Madsen IV* (which is incorrect, as explained above). (Petition at 10.) The decision in *Madsen IV* was not based on the reading of an express preemption clause. Rather, as explained by the Utah Supreme Court in *Madsen IV*, under the Supremacy Clause of the United States Constitution, federal law preempts state law "where it regulates conduct in a field that Congress intended the Federal Government to occupy exclusively" or "to the extent that it actually conflicts with federal law." *Madsen IV* at 903 (*quoting English v. Gen. Elec. Co.*, 496 U.S. 72, 79 (1990)). Thus, in *Madsen IV*, the Utah Supreme Court held that federal regulations in existence in 1975 state that Prudential was not required to pay interest on the mortgage loan reserve account, and these "regulations directly conflict with Madsens' state law claim" and therefore the state law claim for interest is preempted. *Madsen IV* at 904. Thus, the ruling in *Madsen IV* does not implicate *Altria*.

CONCLUSION

This case presents no compelling reason for further review and the Petition for Writ of Certiorari should be denied.

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No. 08-1098

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In The

Supreme Court of the United States

RICHARD MADSEN and NANCY MADSEN,

Petitioners,

vs.

JP MORGAN CHASE BANK, N.A.,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Court Of The State Of Utah

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INTERVENING *WYETH* CASE WARRANTS REMAND

Plaintiffs Richard Madsen and Nancy Madsen (hereinafter collectively referred to as "Madsens") respectfully submit this Supplemental Brief pursuant to Rule 15.8 of the Rules of the Supreme Court of the United States.

Madsens filed their Petition for Writ of Certiorari on March 2, 2009. On March 4, 2009, this Court issued its decision in *Wyeth v. Levine*, 555 U.S. ___, 129 S.Ct. 1187, ___ L.Ed.2d ___ (2009). In that decision, this Court stated, **"[W]e start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress."** *Id.*, 129 S.Ct. at 1194-95. (Internal quotation marks omitted, emphasis added.)[1]

On March 9, 2009, this Court addressed two Petitions for Writ of Certiorari, on cases where the central issue was federal preemption. These cases were *Pennsylvania Employees Benefit Trust Fund v. Zeneca, Inc.*, 499 F.3d 239 (3rd Cir. 2007), and *Colacicco v. Apotex, Inc.*, 521 F.3d 253 (3rd Cir. 2008), respectively.

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[1] On page 9 of their *Petition for Writ of Certiorari*, Madsens cited similar language from *Altria v. Good*, ___ U.S. ___, 129 S.Ct. 538 (2008). But *Wyeth v. Levine*, *supra*, reinforces, emphasizes, and clarifies the similar language from *Altria*, *supra*.

In each of the above cases, this Court granted the Petition for Writ of Certiorari, vacated the judgment, and remanded the action for further consideration in light of *Wyeth v. Levine*. See 2009 WL 578681 (U.S. No. 07-822) and 2009 WL 578582 (U.S. No. 08-437), respectively.

Likewise, this Court should vacate the judgment, and remand the present action to the Utah Supreme Court for consideration in light of *Wyeth v. Levine*, *supra*. Specifically, there is absolutely nothing in the entire **34 year** record of this case to show that it was the "clear and manifest purpose of Congress" to preempt contractual or common law rights of a pledgor-pledgee relationship.

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On Petition For A Writ Of Certiorari To The Supreme Court Of The State Of Utah

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GRANTING CERTIORARI IN THIS CASE WILL SAVE THOUSANDS OR EVEN MILLIONS OF HOURS OF JUDICIAL TIME

Petitioners' (Madsens) core argument is that:

> [C]ertiorari should be granted, so that this Court can give a *stern warning* to lawyers and judges . . . that issues of federal preemption should be heard in the beginning of a case; and not delayed until the *middle* or the *end* of the case.

Petition for Writ of Certiorari at p. 7. (Emphasis in original.)

Prudential's response to the above was simply that:

> However, the desire to give "lawyers and judges" a "stern warning" about the timing of issues in a case is not a "compelling reason[ ]" to grant certiorari.

Brief in Opposition at p. 6.

It is respectfully suggested that the "compelling reason" to grant certiorari is to **save thousands or even millions of hours of judicial time**.

Of course, the instant case is a perfect example. It took **34** years for the Utah courts to make a dispositive ruling on federal preemption. How many other cases out there are 2, or 5, or 8, or 10, or 15

years old; where the trial court judge is holding preemption issues in the background? [1]

Next Prudential tries to argue that the issue of federal preemption was never really delayed. In support of that argument, Prudential gives a *vague reference* to a couple of occasions, over the **34** year history of this case, where the words "federal preemption" were used.

In response to this argument, Madsens refer the Court to footnote 3 (at pp. 7-8) of the original *Petition for Writ of Certiorari*:

> Petitioner is *not* asking this Court to rule on *why* issues of federal preemption were delayed for **34** years in this case. (However, petitioner believes Utah courts did not use the "tools" mentioned in fn. 2 above.) Rather, petitioner simply seeks a ruling that the Utah Supreme Court's *ultimate* decision on federal preemption, after **34** years, was incorrect. But certiorari would also give this Court an opportunity to warn about delays, in general, where federal preemption is an issue. And certiorari would give this Court an opportunity to encourage lower courts to use tools *they already have* to push federal

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[1] Prudential also argues that there is no "compelling reason" to grant certiorari because the federal regulation at issue in this case (12 C.F.R. § 545.6-11) has since been amended. But again, this case is not about the *substance* of 12 C.F.R. § 545.6-11. This case is about *why* issues of federal preemption were sidestepped or delayed for **34** years.

> preemption to the forefront of the litigation. (See fn. 2 above.)

(Emphasis in original.)

In point of fact, the record in this case is over 14,500 pages long. It would be an interesting and exhaustive academic journey to pinpoint exactly *where* or *how* issues of federal preemption were delayed or sidestepped.

But it is not necessary to prove *when* or *how* or even *if* the issue of federal preemption was delayed. It is enough to say that *maybe*, or even *probably*, the lower court sidestepped issues of federal preemption during the **34** year saga. Therefore this Court should correct the ultimate ruling of the Utah Supreme Court on preemption; and at the same time, this Court can warn lower courts not to delay or sidestep issues of federal preemption.

PRUDENTIAL CONTINUES TO IGNORE THE PLAIN RULING OF THE TENTH CIRCUIT

Madsens' *Petition for Writ of Certiorari* is based in part on a conflict between the Utah Supreme Court and the Tenth Circuit Court of Appeals. Specifically, at page 8 of the *Petition*, Madsens argued:

> The conflict is obvious. In *Madsen II*, the Tenth Circuit Court of Appeals concluded that there *was* a contract . . . However, in

> *Madsen IV*, the Utah Supreme Court concluded that there was *no* contract . . .

(Emphasis in original.)

In response, Prudential argued at p. 11 of its *Brief in Opposition* that:

> [T]he Tenth Circuit in *Madsen II* did not hold that a contract to pay interest existed . . .

However, the language of the Tenth Circuit on the contract issue was clear and specific:

> Here the basic issue in the Madsens' complaint is whether *the contract between the Madsens and Prudential* requires the payment of profits or interest on escrowed funds.

Madsen v. Prudential Sav. & Loan Ass'n, 635 F.2d 797, 801 (10th Cir. 1980). (See App. E9 to *Petition for Writ of Certiorari*.) (Emphasis added.)

In summary, the Utah Supreme Court has attempted to overrule the Tenth Circuit Court of Appeals *in this very case*.

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In The

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Individually and on Behalf of
All Others Similarly Situated,

Petitioner,

vs.

JP MORGAN CHASE BANK, N.A.,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Court Of The State Of Utah

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SUBSTANTIAL GROUNDS NOT PREVIOUSLY PRESENTED

Petitioner Nancy Madsen ("Madsen"), individually and on behalf of all others similarly situated, respectfully petitions for rehearing of the order of the Court dated June 8, 2009, denying the *Petition for Writ of Certiorari* to the Utah Supreme Court. This *Petition for Rehearing* is brought pursuant to Rule 44.2 of the *Rules of the Supreme Court of the United States*, based on substantial grounds not previously presented and an intervening circumstance of substantial effect.

1. CERTIORARI SHOULD BE GRANTED TO ENCOURAGE COURTS AND COUNSEL TO CONSERVE JUDICIAL TIME IN FEDERAL PREEMPTION CASES THROUGH THE USE OF INTERLOCUTORY APPEALS.

A. HISTORY OF GROUNDS PREVIOUSLY PRESENTED

Madsen's original *Petition for Writ of Certiorari* (at p. 6) emphasized that federal preemption is the ultimate "trump card." Madsen's original *Petition* (at p. 7) went on to argue that:

> Of course, there are thousands and thousands of other cases pending in courts throughout the United States where federal preemption is an issue. And if judges in those cases delay ruling on preemption, until somewhere in the *middle* or the *end* of the case, **millions of judicial hours will be wasted**.

> In summary, certiorari should be granted, so that this Court can give a *stern warning* to lawyers and judges, throughout the land, that issues of federal preemption should be heard in the beginning of a case – and not delayed until the *middle* or the *end* of the case.

B. SUBSTANTIAL GROUNDS NOT PREVIOUSLY PRESENTED

As stated above, Madsen's original argument was that **millions of judicial hours will be wasted** when issues of preemption are not raised until the end of the case.

In opposition, the Bank (Prudential) has argued that it did not wait until the end of the case to raise the issue of preemption. The Bank (Prudential) asserted that:

> In 1985, on the eve of trial, the trial court denied Prudential's motion for summary judgment which argued that Madsens' claims were preempted by federal regulations.

Brief in Opposition at p. 4, ¶8.

However, when the Bank's (Prudential's) *Motion for Summary Judgment* was denied in 1985, the Bank (Prudential) could have (but did not) file a Petition for Interlocutory Appeal under Rule 5 of the *Utah Rules of Appellate Procedure* (equivalent to 28 U.S.C. § 1292(b), except that the trial court need not grant permission to appeal). If an interlocutory

appeal had been filed, the Utah Supreme Court might have ended the case by 1987 on the identical grounds (federal preemption) that were relied upon by the court in *Madsen IV* in 2008 (*Madsen v. Washington Mutual Bank fsb*, 2008 UT 69, 199 P.3d 898) (Appendix A to *Petition for Writ of Certiorari*). Or stated in other words, **21** years of judicial time could have been saved (between 1987 and 2008) if the Bank (Prudential) had filed a Petition for Interlocutory Appeal in 1985, instead of waiting until 2006 to raise this issue in a cross-appeal.

Although federal circuit courts have encouraged the use of interlocutory appeals,[1] such encouragement by this Court will surely increase the appropriate use of interlocutory appeals in federal preemption cases.[2] And again, **millions of hours of judicial time will be saved** if interlocutory appeals are used more frequently in federal preemption cases.

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[1] See, e.g., *In re Coastal Plains, Inc.*, 179 F.3d 197, 204 (5th Cir. 1999) ("Most unfortunately, Browning did *not* seek certification . . . pursuant to 29 U.S.C. § 1292(b)").

[2] Madsen is not suggesting this Court require a petition for interlocutory appeal every time a motion for summary judgment is denied. But it would be helpful for this Court to point out that this avenue should be considered favorably by attorneys and judges in federal preemption cases.

C. REASONS WHY THE ISSUE OF INTERLOCUTORY APPEAL WAS NOT RAISED IN THE ORIGINAL PETITION FOR WRIT OF CERTIORARI

Madsen's original *Petition for Writ of Certiorari* argued that **millions of judicial hours will be wasted** where judges delay ruling on preemption until the middle or the end of the case.

The purpose of the *Petition for Rehearing* is simply to present one *specific* procedure on *how* the issue of preemption can be resolved early in the case.

D. IMPORTANCE OF CERTIORARI IN THIS CASE

There are literally tens of thousands of federal preemption cases pending around the country. Each federal preemption case is a mixture: A claim under state law **and** the legal question of whether the claim under state law has been preempted (or taken away).

But when the issue of preemption is delayed, the loss of time and extra work for the courts is overwhelming. As stated in *Steel Co. v. Citizens for a Better Environment*, 523 U.S. 83, 112, 118 S.Ct. 1003, 1021, 140 L.Ed.2d 210 (1998) (Breyer, J., concurring), "a more cumbersome system . . . increases . . . the risk of the 'justice delayed' that means 'justice denied.'" The instant case is the perfect example of how decades of court time can be wasted.

Thus the purpose of certiorari in this case is to give guidance and specific procedures on avoiding such horrible delays in reference to preemption cases.

2. CERTIORARI SHOULD BE GRANTED BECAUSE THE UTAH SUPREME COURT ERRED BY CONSTRUING THE TERM "INTEREST" IN A FEDERAL REGULATION TO INCLUDE "PROFITS."

Although there are several issues which Madsen would argue in a brief on the merits in this matter (including issues raised in Madsen's original *Petition for Writ of Certiorari* and in Madsen's briefs before the Utah Supreme Court), Madsen will not repeat all of them in this document. However, the substantial grounds not previously presented to this Court would include one particularly important issue that goes to the merits. That issue is the fact that in *Madsen IV* (*Madsen v. Washington Mutual Bank fsb*, 2008 UT 69, 199 P.3d 898) (Appendix A to *Petition for Writ of Certiorari*), the Utah Supreme Court construed the term "interest" in the federal regulation to include the term "profits" as used by the Utah Supreme Court in *Madsen I* (*Madsen v. Prudential Federal Savings & Loan Ass'n*, 558 P.2d 1337 (Utah 1977)) (Appendix F to *Petition for Writ of Certiorari*).

A. THE APPLICABLE REGULATION ONLY RESTRICTED THE PAYMENT OF "INTEREST."

The pertinent federal regulation (12 C.F.R. § 545.6-11(c))[3] states in part:

> Except as provided by contract, a Federal association shall have no obligation to pay *interest* on escrow accounts apart from the duties imposed by this paragraph. [Emphasis added.]

Madsen I (at 1338, App. F3) dealt with the contractual term "pledged," and found that a pledgor is entitled to an accounting by the pledgee of the profits earned from what was pledged.

> The pledgee has the duty to account to the pledgor for the increase or profits accruing to the pledgee as a result of the possession of the pledged chattel.

Madsen I, at 1340 (See App. F8 to *Petition for Writ of Certiorari.*)

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[3] In *Madsen IV*, the Utah Supreme Court also relied on an older regulation, 12 C.F.R. § 544.1, "Prudential 'is not required to distribute earnings on short-term savings accounts.'" *Madsen IV* at ¶23, App. A15. However, this general rule merely states that the Bank (Prudential) was not *required* by regulation to distribute *earnings*. However, the above language does not prevent the Bank (Prudential) from *voluntarily contracting* to pay *earnings*. (See *Madsen I*, 558 P.2d at 1338, App. F1: "The action is founded upon terms of a deed of trust . . . to determine . . . the legal consequences pursuant to such terms.")

The federal regulation quoted above refers to *interest*, making no mention of *profits* or *earnings*. The plain language of the regulation does not prevent payment of the profits or earnings which the Utah Supreme Court found had to be paid by a pledgee.

B. AN INTERVENING CIRCUMSTANCE OF SUBSTANTIAL EFFECT DEMONSTRATES THE NEED FOR A REHEARING.

Since denying Madsen's *Petition for Writ of Certiorari*, this Court decided the case of *Cuomo v. Clearing House Ass'n, L.L.C.*, ___ U.S. ___, ___ S.Ct. ___, No. 08-453, 2009 WL 1835148. After granting certiorari in that case, this Court pointed out that the terms "visitorial powers" had been interpreted too broadly in their preemptive effect. Likewise the Court should grant certiorari in this case and point out that the term "interest" has been interpreted too broadly in its preemptive effect.[4]

The instant matter and the *Cuomo* case exemplify the need for this Court to emphasize the rule of construction found in *Altria v. Good*, ___ U.S. ___, 129 S.Ct. 538, 543, 172 L.Ed.2d 398 (2008) (internal quotation marks omitted):

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[4] In 2008, the Utah Supreme Court concluded (in the instant case) that a federal regulation governing "interest" payments preempted Madsen's claim for "profits" or "earnings." But if the *Cuomo* case had been available back in 2008, the Utah Supreme Court would have never made such an error.

[W]hen the text of a pre-emption clause is susceptible of more than one plausible reading, courts ordinarily accept the reading that disfavors pre-emption.

Respectfully submitted,

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CERTIFICATION OF COUNSEL

I certify that the *Petition for Rehearing* is presented in good faith and not for delay and is restricted to the grounds specified in Paragraph 2, Rule 44, *Rules of the Supreme Court of the United States*.

July 2, 2009
Date

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